

PUBLIC  
DIRECT TESTIMONY  
of  
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Policy Program  
Policy Division  
Illinois Commerce Commission

Petition to Review Affiliate Interactions with Peoples Energy Home Services  
pursuant to January 10, 2012 Rate Order and Investigation into interactions with affiliates

North Shore Gas Company and The Peoples Gas Light and Coke Company

Docket Nos. 12-0273/13-0612 (Cons.)

August 21, 2014

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1   **I.     Witness Qualifications**

2   **Q.     Please state your name and business address.**

3   A.     My name is David Sackett. I am employed by the Illinois Commerce  
4           Commission, 527 East Capitol Avenue, Springfield, Illinois, 62701.

5  
6   **Q.     What is your current job title?**

7   A.     I am employed as an Economic Analyst in the Policy Program of the  
8           Policy Division of the Illinois Commerce Commission ("Commission" or  
9           "ICC").

10

11   **Q.     What are your responsibilities within the Policy Division – Policy**  
12           **Program?**

13   A.     I provide economic analysis and advise the Commission and other Staff  
14           members on issues involving the utility industries. I review tariff filings and  
15           make recommendations to the Commission concerning those filings. I  
16           provide testimony in Commission proceedings. I am one of the primary  
17           Staff experts on affiliate issues.

18

19   **Q.     State your educational background.**

20   A.     I graduated from Kankakee Community College with an Associate of  
21           Science degree in Arts and Sciences in 1998. I graduated with highest  
22           honors from Illinois State University with a Bachelor of Science degree in  
23           Economics and History in 2000. I obtained a Master of Science degree in

Applied Economics from Illinois State University in the Electric, Natural Gas and Telecommunications Economics sequence in 2002.<sup>1</sup> I also completed an internship at the Commission in the Energy Division in 2001.

**Q. Describe your professional experience.**

A. Since July 2007, I have been an Economic Analyst in the Policy Program of the Commission's Energy and Policy Divisions. During that time I have participated in numerous docketed proceedings before the Commission. Of particular note has been my testimony dealing with affiliate issues. Most recently, I filed testimony in Nicor Gas Company's Operating Agreement docket (Docket No. 09-0301 consolidated with Docket No. 11-0046, in which Nicor Gas Company sought approval of its reorganization), Docket Nos. 11-0280 and 11-0281 (Cons.) (North Shore Gas Company and The Peoples Gas Light and Coke Company rate proceedings), Docket Nos. 11-0561/0562/0563/0564/0565/0566 (Cons.) (the rate proceeding for certain Utilities Inc. water companies), Docket No. 11-0767 (the Illinois-American Water Company rate proceeding), Docket No. 12-0299 (North Shore Gas Company and The Peoples Gas Light and Coke Company proposal to enter into an affiliated interest agreement with its affiliate ITF) and Docket Nos. 12-0511 and 12-0512 (Cons.) (North Shore Gas

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<sup>1</sup> "The Electricity, Natural Gas, and Telecommunications Sequence is a structured program that combines training in basic economic theory and statistical methods with specialized training in the theory, history and institutions of the economics of regulation." <http://www.econ.ilstu.edu/grad/program.htm>.

Company and The Peoples Gas Light and Coke Company rate proceedings).

Prior to joining the Commission, I was an instructor at Illinois State University from 2003 to 2006, where I taught various courses in economics and statistics to undergraduate students. I retired in July of 2014 as a Major from the Marine Corps Reserve after more than 21 years of service in the Infantry; I have completed two combat deployments to Iraq.

**II. Purpose of Testimony and Background Information**

**Q. What is the subject matter of your direct testimony?**

A. This testimony concerns an investigation requested by Staff and ordered by the Commission into The Peoples Gas Light and Coke Company's ("Peoples Gas") and North Shore Gas Company's ("North Shore") (jointly, "Companies") interactions with their various affiliates. My testimony also responds to the direct testimony of Companies' witnesses Ms. Linda M. Kallas (NS-PGL Ex. 1.0) and Mr. Jerard Julian (NS-PGL Ex. 2.0) filed in Docket No. 12-0273.

**Q. Do you have any attachments to your testimony?**

A. Yes. I have attached the following to my testimony:

**Table 1 – List of Attachments**

Att	Source

A	Email from Allan. Ikoma, Manager, Rates for Peoples Gas and North Shore to Joan Howard, March 24, 2003
B	North Shore Data Request ("DR") response from 2004
C	Companies Response to Staff DR Docket Nos. 11-0280/0281 (cons.) DAS-10.01
D	Companies Response to Staff DR Docket Nos. 11-0280/0281 (cons.) DAS-9.09
E	Companies Response to Staff DR DAS-13.01
F	Companies Supplemental Response to Staff DR DAS-13.05
G	Companies Response Staff DR DAS- 19.03
H	Companies Response to Staff DR Docket Nos. 11-0280/0281 (cons.) DAS-2.12
I	Companies Response to Staff DR DAS-19.01
J	Companies Response to Staff DR Docket No. 12-0299 DAS-1.01
K	Companies Response Staff DR DAS-24.02
L	Companies Response to Staff DR DAS-20.01
M	Companies Response to Staff DR DAS-14.09
N	Companies Supplemental Response to Staff DR DAS-10.19
O	Companies Response to Staff DR DAS-15.02
P	Companies Confidential Response to Staff DR DAS-10.18
Q	Companies Response to Staff DR Docket Nos. 12-0511/0512 (cons.) DAS-7.02
R	Companies Response to Staff DR DAS-23.03
S	Companies Response to Staff DR DAS-10.19

T	Companies Supplemental Response to Staff DR DAS-18.01
U	Companies Response to Staff DR RWB-1.03 (CONF)
V	Peoples Gas Response to Staff DR Docket Nos. 12-0511/2c.DAS-11.04
W	Peoples Gas Response to Staff DR Docket Nos. 12-0511/2c.DAS-10.01 (CONF)
X	Companies Response Staff DR DAS-25.02
Y	Companies Response to Staff DR DAS-26.02
Z	Companies Response to Staff DR DAS-22.02
AA	Companies Response to Staff DR Docket No. 12-0299 DAS-7.02
AB	Companies Supplemental Response to Staff DR DAS-18.03
AC	Companies Third Supplemental Response to Staff DR DAS-10.12
AD	Companies Response to Staff DR DAS-26.04
AE	Companies Response to Staff DR DAS-18.02
AF	Companies Supplemental Response to Staff DR DAS-23.01
AG	Companies Response to Staff DR DAS-21.04
AH	Companies Response to Staff DR DAS-16.01
AI	Companies Supplemental Response to Staff DR Docket No. 12-0299 DAS-7.01
AJ	Peoples Gas Response to Staff DR Docket No. 12-0299 DAS-9.02
AK	Companies Supplemental Response to Staff DR DAS-11.01
AL	Companies Response to Staff DR DAS-15.03
AM	Companies Response to Staff DR DAS-15.11

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**III. Summary of Conclusions and Recommendations**

**Q. Please summarize your conclusions and recommendations.**

A. Through affiliate interest transactions, the Companies have a history of abuses of the public interest that require the Commission to act now to protect the public interest going forward. In particular, Peoples Gas has acted against the public interest as follows:

1. Peoples Gas provided services for Peoples Natural Gas Vehicle Corporation ("PNGV Corp." under the Intercompany Service Agreement ("ISA") that were not provided at cost as required by the ISA.

2. Peoples Gas interacted with Pinnacle CNG Systems, LLC ("Pinnacle") preferentially before it became an affiliate.

3. Peoples Gas interacted with Pinnacle after it became an affiliate under an agreement that had not been approved by the Commission.

4. Peoples Gas interacted with Pinnacle under the Services and Transfers Agreement ("STA") after it became an affiliate but before it was properly added to the STA.

5. Peoples Gas interacted with Integrys Transportation Fuels after it became an affiliate but before it was properly added to the STA.

6. Peoples Gas attempted to include in its rates costs for Pipeline Protection Program ("PPP") solicitation services provided by Integrys Business Support ("IBS") at no charge to Peoples Energy Home Services ("PEHS").

7. Peoples Gas charged PEHS PPP billing charges below cost by not increasing those charges when postage rates increased.

8. Peoples Gas increased charges for repairs to customer-owned piping to ratepayers at an amount that more than double its costs and charged PEHS PPP repairs charges at cost. This provided PEHS with a competitive advantage by disadvantaging ratepayers.



9. Peoples Gas discriminated against ratepayers who did not purchase PPP in the provision of repairs to customer-owned piping by providing firm<sup>2</sup> repair services to PEHS but not ratepayers without PPP.

Similarly, North Shore has acted against the public interest as follows:

1. North Shore attempted to include in its rates costs for PPP solicitation services provided by IBS at no charge to PEHS.

2. North Shore charged PEHS billing charges for PPP below cost by not increasing those charges when postage rates increased.

3. North Shore increased charges for repairs to customer-owned piping to ratepayers more than double its costs and charged PEHS PPP repairs charges at cost. This provided PEHS with a competitive advantage by disadvantaging ratepayers.

4. North Shore discriminated against ratepayers who did not purchase PPP in the provision of repairs to customer-owned piping by providing firm repairs services to PEHS but not ratepayers without PPP.

It is my opinion that the current set of Affiliated Interest Agreements ("AIAs") does not adequately protect that public interest and that modifications are necessary to prevent further abuse. The Commission should increase its oversight of these affiliate transactions going forward.

Therefore I recommend for the Commission take the following actions:

Rec. 1. Require that the Master Affiliated Interest Agreement ("Master AIA"), that was approved in Docket No. 10-0408 be modified by adding a Rider applicable to all Integrys Utilities in Illinois which stipulates that the Companies will only provide services to and receive services under the Master AIA from regulated affiliates (as outlined in Section C.I) and the

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<sup>2</sup> Firm repair services are those provided without interruption or in every case requested.

Companies will not provide services to nor receive services from unregulated affiliates (as outlined in Section C.II). Thus, any interactions with any unregulated affiliates, apart from the IBS Regulated AIA, would require direct Commission approval.

Rec. 2. Prohibit any affiliate or its agent from using information, including but not limited to ratepayer lists, received or developed pursuant to the provision of services to the Companies from soliciting, marketing or otherwise attempting to provide any product or service directly or indirectly to the Companies' ratepayers or providing such information to any third party whether affiliated with the Companies or not.

Rec. 3. Consider whether fines should be imposed upon the Companies for specific Company actions set forth below which violated the Act to discourage future improprieties by the Companies and/or other utilities.

#### **IV. Introduction and Background**

##### **A. Profit-maximizing firms**

**Q. How can comparing the incentives that profit-maximizing utility faces with those incentives that an unregulated firm faces provide valuable perspective?**

A. To understand the effect the corporate relationship has on the behavior of utilities, one can compare the actions of a normal profit-maximizing firm with those actions that a profit-maximizing utility takes under certain circumstances. Adding in corporate relationships illustrates the complexities required to protect the public interest.

**Q. How do profit-maximizing utilities typically behave?**

A. Profit-maximizing firms generally behave in a manner consistent with maximizing profits subject to certain constraints. A rate-regulated utility ("Utility") is a profit-maximizing firm or business that seeks to maximize its profits. When a Utility interacts with an unaffiliated firm, it often seeks to get the best deal that it can for its bottom line.

**Q. How do incentives change when a Utility is part of a utility holding corporation?**

A. If the Utility is a part of a utility corporation holding company, then it generally seeks to maximize the collective profit of the utility holding company and all of its subsidiaries and affiliates. Thus, the incentives for a Utility that is part of a utility holding company differ from those of a profit maximizing firm with no affiliates.

**Q. Please describe some behavior that a Utility might engage in that would raise the collective profits of its utility holding company and its subsidiaries and affiliates.**

A. A Utility can take actions to increase the collective profits of it and its subsidiaries and affiliates if the regulated Utility interacts with its parent and affiliates such that profits accrue to affiliates that are unregulated rather than to the Utility subject to regulatory earnings constraints. This involves, for example, the shifting of cost from the unregulated affiliate to the Utility or conversely, the shifting of revenues from the Utility to its affiliates. A Utility

can also positively affect the holding company bottom line by shifting risk from unregulated affiliates to itself. The Utility can also leverage any market advantage it has (e.g., by being the sole distributor of gas in an area) to provide preferential treatment that allows the affiliate to gain a competitive advantage in some other market.

**B. Affiliated Interests and the Public Utilities Act**

**Q. Are Utilities un-restrained in succumbing to these incentives?**

A. No. There are legal requirements and regulatory and ethical pressures that constrain the actions of Utilities.

**Q. Please describe the regulatory pressures relating to transactions with affiliates.**

A. Utilities face considerable pressure from various regulatory agencies that regulate the utility's actions. This regulatory oversight pressures Utilities to act within the law, even when it may not be the most financially beneficial option.

**Q. Please describe the ethical pressures requirements regarding transactions with affiliates.**

A. In addition to the regulatory pressures that Utilities face, there also ethical actions that individual employees play in following the law, corporate policy

and Utility policy. Not all employees are willing to compromise their own morals or ethical principles to make the corporation more profitable, despite the personal benefits such profit would have for them.

**Q. How does the Public Utilities Act (“Act”) govern the interactions between public utilities and their affiliated interests?**

A. While I am not an attorney, it is my understanding that the Act imposes requirements with respect to interactions between public utilities and their affiliates. For instance, Section 7-101 of the Act governs transactions between public utilities and their affiliates. It provides that no contract between a Utility and its affiliate is effective until it has been filed with and consented to or excepted by the Commission.

No management, construction, engineering, supply, financial or similar contract and no contract or arrangement for the purchase, sale, lease or exchange of any property or for the furnishing of any service, property or thing, hereafter made with any affiliated interest, as hereinbefore defined, shall be effective unless it has first been filed with and consented to by the Commission or is exempted in accordance with the provisions of this Section or of Section 16-111 of this Act. The Commission may condition such approval in such manner as it may deem necessary to safeguard the public interest. If it be found by the Commission, after investigation and a hearing, that any such contract or arrangement is not in the public interest, the Commission may disapprove such contract or arrangement. Every contract or arrangement not consented to or excepted by the Commission as provided for in this Section is void.

220 ILCS 5/7-101(3) (emphasis added).

**Q. Does this subsection apply equally to services provided by the Utility**

**to the affiliate as well as to services provided by the affiliate to the Utility?**

A. Yes. While I am not an attorney, I understand that Section 7-101 applies to all transactions between Utilities and their affiliates regardless of which entity provides services to the other, unless notice of those transactions are filed with and consented to by the Commission or are excepted in accordance with the provisions of Section 7-101 or of Section 16-111 of the Act.

**Q. What types of approval does the Act allow?**

A. The Act allows the Commission some flexibility in its approval. First, in accordance with the Act, the Commission has set forth rules governing the interactions between Utilities and their affiliates. These rules provide additional guidance on what is an acceptable transaction. The rules allow the waiver of filing and the waiver for consent and approval of certain contracts. 83 Ill. Admin Code Part 310. Second, the Commission can provide blanket / generic approval of transactions for certain types of services provided according to specific charges through agreements called Affiliated Interest Agreements or ("AIAs"). Any contract or arrangement that does not fall into one of the above mutually exclusive categories must be approved by the Commission or the contract or arrangement is not effective and void.

255 **Q. Please describe AIAs further.**

256 A. AIAs refer to general agreements that allow for an on-going provision of  
257 services between affiliates. AIAs may also provide for sub-agreements for  
258 the services approved by the Commission in the AIA and for charges in  
259 compliance with the terms of the AIA to be entered into with parties to the  
260 AIA without subsequent Commission approval.

261

262 **Q. What is a service company?**

263 A. A service company provides services such as customer service or  
264 accounting to other affiliates. In most cases this service company is part of  
265 a Utility's holding company system. In some cases, those service  
266 companies provide services to only regulated affiliates. In other cases,  
267 however, those service companies provide services for regulated and  
268 unregulated affiliates alike. In the latter case, the potential for subsidization  
269 of unregulated affiliates by the Utilities increases.

270

271 **Q. Are the Companies currently parties to any AIAs?**

272 A. Yes. The Commission has approved several AIAs for Peoples Gas and  
273 North Shore. The Commission has approved an agreement between the  
274 Companies and the Integrys corporate service company IBS called the IBS  
275 Reg AIA in Docket No. 07-0361.<sup>3</sup> Additionally, the Commission approved

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<sup>3</sup> This AIA is the primary agreement by which the Companies receive services from its affiliate IBS. It is a one-way agreement in which IBS provides the Companies for services but not vice-versa.

the current general AIA<sup>4</sup> that affects services between Peoples Gas, North Shore, and all their Integrys affiliates which is referred to as the Master AIA, in Docket No. 10-0408<sup>5</sup>.

**Q. Are there any other AIAs that are relevant to this investigation?**

A. Yes. The Commission approved the ISA in Docket No. 55071 between the Companies and Peoples Energy Corporation and several of its subsidiaries. Later, the ISA was replaced by the STA between the Companies and Peoples Energy Corporation and all of its subsidiaries which was approved by the Commission in Docket No. 06-0540.<sup>6</sup> The STA was then replaced by the Master AIA.

**Table 2 – The Companies’ Significant AIAs**

Name	Docket No.	Significant Parties	Effective dates	Cost Basis
ISA	55071	Peoples Gas North Shore and PEC	8/1/1969 - 2/6/2007	Reasonable Cost
STA	06-0540	Peoples Gas North Shore and PEC	7/2007 - 12/31/2013	FDC
IBS Non-reg	07-0361	Peoples Gas	12/7/2007 -	FDC

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<sup>4</sup> Called the Non-IBS AIA.

<sup>6</sup> The STA was in effect from 2/7/2007 to 12/31/2013.



AIA		North Shore and IBS	Current	
Master AIA	10-0408	Peoples Gas North Shore and all Integrys affiliates	1/1/2014 - Current	Market or FDC

288

289 **C. Issues leading to the investigation.**

290 **Q. What events precipitated this investigation?**

291 A. In Docket Nos. 11-0280/0281 (Cons.), I raised several objections to the  
292 Companies support of an unregulated affiliate Peoples Energy Home  
293 Services (“PEHS”) and its Pipeline Protection Plan (“PPP”) gas line warranty  
294 product. See North Shore Gas Co. and The Peoples Gas Light and Coke  
295 Co., ICC Final Order Docket Nos. 11-0280/0281 (Cons.), 88-98(January 10,  
296 2012) (“2011 Rate Case”). The Commission ordered an adjustment and  
297 directed an investigation into the Companies continued support of PEHS.  
298 Id. at 98. That investigation began as Docket No. 12-0273. Subsequent to  
299 that order, I became aware of additional affiliate interactions that did not  
300 appear to be in the public interest. I filed a Staff Report requesting that the  
301 Commission expand the scope of this investigation to consider all affiliate  
302 interactions and remedies. The Commission ordered an expansion of the  
303 investigation as Docket No. 13-0612 and that the two investigations be

consolidated. North Shore Gas Co. and The Peoples Gas Light and Coke Co., ICC Order Initiating Proceeding Docket No. 13-0612, 2 (November 6, 2013).

**Q. Did the Companies file testimony with its initial filing in Docket No. 12-0273?**

A. Yes. The Commission ordered the Companies to address two issues in testimony: solicitation of ratepayers for affiliated products and repair charges to ratepayers not on PPP. I will address all issues relating to the Companies direct testimony in Docket No. 12-0273 below in the section related to PEHS.

**V. The Companies interactions with unregulated affiliates that are not in the Public Interest**

**Q. Please indicate which instances of the Companies' interactions with their affiliates that you believe are not in the public interest.**

A. There have been several instances of improprieties found by the Commission. Following an evaluation of the factual circumstances in each matter, the Commission found impropriety between the Companies and their affiliate Peoples Energy Home Services (2011 Rate Case Final Order at 93) and between Peoples Gas and its affiliate Enovate, LLC., ("enovate") a company jointly owned by Peoples Energy Corporation and Enron (The Peoples Gas Light and Coke Co., ICC Final Order Docket No.

01-0707, 144 (March 28, 2006)). Below, I discuss the history of these inappropriate interactions and provide evidence regarding additional improprieties between the Companies and PEHS. Additionally, I have uncovered evidence of behavior inconsistent with the public interest with respect to Peoples Gas and two affiliates in the Compressed Natural Gas (“CNG”) services industry – Pinnacle and PNGV Corp., which I explain further below.

**A. Improper interactions with affiliates by Peoples Gas and North Shore.**

**Q. Has the Commission ever found the Companies to have engaged in improper behavior with affiliates?**

A. Yes. There have been at least two instances of impropriety by the Companies which the Commission has clearly reviewed the record and found against them. The most recent example of this is the Companies and their affiliate IBS and the interaction of these firms with PEHS. The second example is the interaction of Peoples Gas with enovate. Below, I explain these improper interactions with PEHS and provide additional evidence regarding improper interactions between the Companies and PEHS not previously presented to the Commission.

**1. Peoples Energy Home Services and the Pipeline Protection Plan**

**Q. Please describe the history of the relationship between the Companies, Peoples Energy Home Services, and its Pipeline Protection Plan?**

A. In March 2003 Peoples Gas and North Shore approached the Commission Staff to inform them of their intent to create a gas line warranty program to be offered by the Companies. (Attach. A, Email from Allan. Ikoma, Manager, Rates for Peoples Gas and North Shore to Joan Howard, March 24, 2003.) In 2004, the Companies informed Staff that instead of being offered by the Companies, PEHS was offering the gas line warranty program. "The parent company, Peoples Energy Corporation, reviewed options for offering the service and considered potential risks (losses), and rewards (profits) and determined that the best interests of shareholders and ratepayers would be served in offering the program, for both PGL and NGS through PEHS." (Attach. B, North Shore Data Request ("DR") response from 2004.)

**Q. What services did the Companies provide for PEHS?**

A. From 2004 to 2007, the Companies provided billing, repairs, solicitation, customer service and marketing services to PEHS in support of PEHS warranty products, mainly PPP, a warranty on in-side gas lines. PEHS had no employees and was, thus, dependent upon the Companies to perform these services. All interactions between the Companies and

PEHS were governed initially pursuant to the ISA and subsequently under the STA.<sup>7</sup> Both AIAs required that PEHS pay the Companies' for all services provided by the Companies' to PEHS at cost.

From 2008 to 2012, the Companies continued to provide repairs, while IBS provided billing, solicitation, and customer service to PEHS.<sup>8</sup>

**Q. When did the issue of the Companies' charges to PEHS become a matter of interest to the Commission?**

A. In the 2011 Rate Case, the Companies admitted that IBS had failed to charge PEHS for either solicitations or customer service from 2008 through August 2011. (Attach. C, Companies Response to Staff DR Docket Nos. 11-0280/0281 (Cons.) DAS-10.01(b).) The Companies indicated the problem had been corrected and IBS would charge PEHS appropriately going forward. (Attach. D, Companies Response to Staff DR Docket Nos. 11-0280/0281 (Cons.) DAS-9.09.)

**Q. Did the Commission's Final Order in the 2011 Rate Case address the issue of solicitation charges to PEHS?**

A. Yes; the Commission determined that IBS had not charged PEHS for solicitation expenses, and ordered an adjustment:

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<sup>7</sup> After February 7, 2007.

<sup>8</sup> IBS provided services to PEHS under the IBS Non-Reg AIA which requires all services to be provided at Fully Distributed Cost.

The Commission agrees with Staff and accepts Staff witness Sackett's proposed adjustment to the expenses billed to the Companies from their affiliated service company IBS. The evidence supports the conclusion that IBS failed to charge PEHS for services IBS performed for it related to the PPP according to its effective affiliate agreements and failed to credit the Companies for those revenues. This failure by IBS to recognize revenues for services it provides to certain affiliates does, in fact, have the end result of IBS over charging the Companies for services provided by IBS to the Companies. We find that Staff's adjustment based on the margin of \$656,267 and \$116,361 that PEHS makes on PPP for Peoples Gas and North Shore reasonable.

2011 Rate Case Final Order at 93.

**Q. Did the Commission's Final Order in the 2011 Rate Cases address the issue of an investigation of the Companies' interactions with affiliates?**

**A.** Yes. The Commission found that the Companies acted improperly with their affiliates to the detriment of ratepayers and ordered an investigation to prevent continuing subsidization of affiliates by ratepayers. The Commission ordered this investigation, as requested by Staff, stating:

The Commission agrees with Staff and finds that the Utilities have not properly interacted with their affiliates as evidenced by our conclusions in the above related sections. Staff's proposal for further Commission investigation of the Utilities' interactions with their affiliates is warranted and in the public interest. We believe that the investigation is necessary to prevent ratepayers from continuing to subsidize the affiliates. On December 15, 2010, this Commission approved a Master Affiliated Interests Agreement (Master "AIA") by its Order in Docket No. 10-0408 that has not yet become effective. The Companies argue that the Services and Transfer Agreement ("STA") is still in effect and allows the Utilities to provide the solicitation services for the nonregulated affiliates; however, the language that specifically allows the provision of

solicitation services is not included in the Master AIA. Since it is now clear that the Utilities intend to continue the provision of solicitation services even under the Master AIA when it becomes effective and the Commission finds that the Utilities have not properly interacted with their affiliates in the provision of services under the STA, it is necessary for the Commission to render a more direct conclusion on the provision of solicitation services to affiliates.

Id. at 98.

**Q. What new information about PEHS was provided by the Companies in their direct testimony filed in Docket No. 12-0273?**

A. The Companies' direct testimony informed the parties and the Commission of the discontinuation of PPP in 2012. (NS-PG Ex. 1.0, 3, 11.) Subsequently, a data request response indicated that IBS ceased solicitation of PPP on June 8, 2012. (Companies Response to Staff DR DAS-1.03(c).) PEHS sent letters (Companies Response to Staff DR DAS-3.01(e) Attach 01) to its customers notifying them of the end of PPP on July 16, 2012 (Companies Response to Staff DR DAS-16.04(b)).

**Q. What is the Companies' assertion regarding IBS charges to PEHS following the Commission's order to do so in the 2011 Rate Case?**

A. Ms. Kallas states that IBS "charges PEHS at cost." (NS-PG Ex. 1.0, 10.)

**Q. Is this statement by Ms. Kallas that IBS charged PEHS at cost correct? Please explain.**

456 A. No. The materials provided by the Companies in response to data requests  
457 show that Ms. Kallas' response is incorrect. First, when Ms. Kallas' direct  
458 testimony was filed in April 2012, IBS was not charging PEHS for on-going  
459 solicitation services. (Attach. E, Companies Response to Staff DR DAS-  
460 13.01(a).) Though the Companies had indicated the problem had been  
461 corrected and IBS would charge PEHS appropriately going forward, IBS  
462 never followed through on that promise. (Attach. D, Companies Response  
463 to Staff DR Docket Nos. 11-0280/0281 (Cons.) DAS-9.09(c).) Second, IBS  
464 never went back and required PEHS to pay for the 3 missed years. (Attach.  
465 F Attach 02 to the Companies Supplemental Response to Staff DR DAS-  
466 13.05.) When IBS finally did charge PEHS for service, it ended up charging  
467 PEHS only \$18,507 for what amounted to four and a half years of  
468 solicitation. IBS budgeted \$16,572 for a single year for the 2012 test year.  
469 2011 Rate Case Final Order at 88. Thus, the final billing reflects a  
470 significant reduction from the budget. Third, IBS never charged PEHS for  
471 overheads<sup>9</sup> for any of the four and a half years that it provided services to  
472 PEHS.<sup>10</sup> (Attach. F, Attach 02 to the Companies Supplemental Response to  
473 Staff DR DAS-13.05.) Fourth, while solicitation of new customers ceased in  
474 June 2012, IBS continued to provide call center services to active customers  
475 through September 2012 and invited calls to the call center to discuss the  
476 closing. (Companies Response to Staff DR DAS-3.01(e) Attach 01.) It is

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<sup>9</sup> Overheads refers to labor related costs such as pension and health insurance as well as the physical plant structures that are needed to provide services.

<sup>10</sup> Strangely, the Companies bemoan the fact that they inadvertently overcharged PEHS for July 2012. (Attach. E, Companies Response to Staff DR DAS-13.01(a).)



reasonable to assume that this would have increased the number and proportion of calls from PPP customers.

**Q. Do you have a conservative estimate for IBS's customer relations costs for PEHS?**

A. Yes. I have used the budget numbers provided by IBS and extrapolated the charges and overheads for each of the years that IBS provided those services. My conservative estimate of those costs is \$124,916. Since IBS actually billed PEHS only \$18,506 over this entire period, PEHS paid less than 15% of these costs. The remaining 85% were absorbed by regulated utilities, including Peoples Gas and North Shore. While Staff was able to get an adjustment for these costs in the 2011 Rate Case, rates from the 2009 Rate Case were not adjusted and included those costs. So ratepayers paid for services provided to PEHS during this time.

**Table 3 – Estimated Cost of Customer Care**

Customer Care				
	Estimated Costs for PEHS			
	Amount			
Year	w/o overheads	Overheads	Total	
Calendar 2008	\$ 25,468 <sup>11</sup>	\$ 4,982 <sup>12</sup>	\$ 30,450	
Calendar 2009	\$ 25,468 <sup>13</sup>	\$ 4,982 <sup>14</sup>	\$ 30,450	
Calendar 2010	\$ 25,468	\$ 4,982 <sup>15</sup>	\$ 30,450	
Calendar 2011	\$ 18,563	\$ 3,631 <sup>16</sup>	\$ 22,194	

<sup>11</sup> Estimated using budget amount for 2010. (DAS-13.05 Attach 02)

<sup>12</sup> Overhead estimated using 2012 budget percent of 19.6%. (DAS-13.05 Attach 02)

<sup>13</sup> Estimated using budget amount for 2010. (DAS-13.05 Attach 02)

<sup>14</sup> Overhead estimated using 2012 budget percent of 19.6%. (DAS-13.05 Attach 02)

<sup>15</sup> Overhead estimated using 2012 budget percent of 19.6%. (DAS-13.05 Attach 02)

<sup>16</sup> Overhead estimated using 2012 budget percent of 19.6%. (DAS-13.05 Attach 02)

Calendar 2012	\$ 14,268	\$ 2,791	\$ 11,373 <sup>17</sup>	19.6%
Total	\$ 109,235	\$ 11,404	\$124,916	
Paid by PEHS	\$ 18,507		14.8%	

**Q. What does Table 3 – Estimated Cost of Customer Care illustrate regarding Integrys and IBS affiliate transactions?**

A. Though the amounts are small, they illustrate Integrys and its affiliates are either incapable or unwilling to follow the requirements of agreements in place to ensure that subsidization does not occur.

**Q. Even though neither of the Companies nor IBS are still soliciting for PEHS, is the issue of solicitation moot?**

A. No. Given the Companies track record with PEHS, I do not think that the Companies should be allowed the option to continue solicitation in the future. As noted above, the Final Order in the 2011 Rate Case requires that this investigation consider the provision of solicitation services to any affiliates, not only PEHS. Thus, the Commission should determine if further solicitation of the Companies ratepayers under the Master AIA is in the public interest.

**Q. What does the Master AIA state regarding solicitation for affiliates?**

A. The Master AIA has two distinct lists of services, one between regulated affiliates and another between regulated and unregulated affiliates. The

---

<sup>17</sup> This number is 8/12<sup>th</sup> of the budgeted amount because IBS only provided service through August 2012.

Master AIA lists solicitation, called “marketing and sales work” as a service that can be provided to or received from regulated affiliates and that same service is absent from the section of services that can be provided to unregulated affiliates.

Appendix C – Services

Subject to the limitations set forth in Section 1.1 and applicable state and federal requirements, a Party may provide to or receive from any other Party the Services described in this Appendix C.

“Major Services” shall mean Services identified as such in this Appendix C and for which Parties expect that, in the normal course of business and under normal operating conditions, they shall provide on a regular or day-to-day basis. “Incidental Services” shall mean Services identified as such in this Appendix C and for which the Parties expect that, in the normal course of business and under normal operating conditions, they shall provide infrequently or, if provided on a regular or day-to-day basis, shall represent an insignificant amount of intercompany services provided by the Providing Party.

I. Any Regulated Party may provide to or receive from any other Regulated Party the following Services:

Major Services....

3. Customer: Provide customer service; support billing and payment processing; support credit and collections activity; energy conservation support; marketing and sales work.

II. Any Non-Regulated Party may provide to or receive from any Regulated Party the following Services:

Incidental Services....

4. Customer: Provide customer service; support billing and payment processing; support credit and collections activity.

(Attachment to Companies Response to Staff DR DAS-11.04.)

**Q. How did the Companies first address issue of solicitation going forward under the Master AIA?**

549 A. The Companies initially interpreted the Master AIA to give them the right to  
550 solicit for unregulated affiliates. Despite clear difference in the listed  
551 services under the category “Customer,” the Companies chose to read that  
552 agreement to mean the opposite of what it says. “Please see Appendix C of  
553 the Master AIA[ ]. Appendix C includes customer services among services a  
554 non-regulated party may provide to or receive from a regulated party. A non-  
555 regulated party may provide any service to another non-regulated party.”  
556 (Companies Response to Staff DR DAS-1.01(n) (internal references  
557 omitted).) By expanding the scope of the defined term “Customer,” the  
558 Companies found support in the AIA to allow them to provide these services.

559

560 **Q. How did the Companies next address issue of solicitation going**  
561 **forward under the Master AIA?**

562 A. At the same time that the Companies agree to interpret the Master AIA as it  
563 clearly read<sup>18</sup> (Companies Supplemental Response to Staff DR DAS-  
564 3.01(a)), they assert that they cannot control the actions of their affiliate that  
565 provides call center services on their behalf from soliciting their ratepayers  
566 for other goods and services for other third parties after completing the  
567 official business of the call.

---

<sup>18</sup> North Shore and Peoples Gas agree that neither shall construe the term “Customer” as used in Section II of Appendix C of the Master AIA (Attachment 5 of the response to Staff data request DAS 1.01) to include any of the following: marketing, sales, customer solicitation. Section II addresses services that a Non-Regulated Party may provide to or receive from a Regulated Party. Under the Master AIA, North Shore and Peoples Gas shall not provide marketing, sales or solicitation service to a non-utility affiliate or receive such services from a non-utility affiliate. Supplemental Companies Response to Staff DR DAS-3.01a)

North Shore and Peoples Gas believe that Integrys Business Support, LLC ("IBS") may, while taking a telephone call from a North Shore or Peoples Gas customer or prospective customer, on that utility's toll-free telephone line or any telephone line, during that same call, solicit on behalf of or otherwise provide services for Peoples Energy Home Services ("PEHS"). (Companies Response to Staff DR DAS-3.01(f).)

**Q. Did the Companies finally agree in a data request response to prohibit solicitation going forward under the Master AIA?**

A. Yes. The Companies finally agree that they can assert control over IBS interactions with Company ratepayers. "North Shore and Peoples Gas agree that they will direct IBS not to solicit their customers for services offered by non-utility affiliates for the time being, *i.e.*, subject to an order in this case." (Companies Response to Staff DR DAS-6.01.)

**Q. Did the Companies finally agree in a data request response to prohibit provision of customer information to any affiliate?**

A. Yes. At Staff's request, the Companies also agreed to "not provide customer information to any affiliate and to instruct IBS to not provide customer information to any affiliates." (Companies Response to Staff DR DAS-6.01.)

**Q. Did you testify in the Companies' 2011 Rate Case regarding the issue of charges for repair services provided by the Companies on behalf of PEHS?**

594 A. Yes. As I indicated in my direct testimony in the 2011 Rate Case, the  
595 Company charged rates to its ratepayers for in-home repairs that were  
596 about twice as much as they charged their affiliate PEHS for the same  
597 services. (See 2011 Rate Case, Staff Ex. 18.0, 25.)

598

599 **Q. What was the Commission's finding in the Companies' 2011 Rate**  
600 **Case regarding the issue of charges for repair services provided by**  
601 **the Companies on behalf of PEHS?**

602 A. The Commission determined that the Companies had under-charged its  
603 affiliates for repair services, leading to higher rates for ratepayers, and  
604 ordered an adjustment. The Commission also required that the  
605 Companies charge their affiliate the same repair charges that ratepayers  
606 were paying:

607

608 The STA requires that the Utilities charge their affiliates the  
609 pricing mechanism approved by the Commission or, if none  
610 exists, the FDC of providing that service. We find that since  
611 the Companies have not charged the FDC of providing the  
612 repair service, we are now placed in a position to approve an  
613 alternate pricing mechanism. The Commission agrees with  
614 Staff and finds that its adjustments are reasonable. The  
615 Utilities shall charge PEHS the same rate that they charge  
616 ratepayers. Further, the full amount of these repairs should be  
617 included in the test year for Peoples Gas and North Shore  
618 respectively.

619

620 2011 Rate Case Final Order at 97.

621

622 **Q. How did the Companies respond to the Commission's direction that**  
623 **the Companies provide an explanation of the charges to ratepayers**  
624 **and charge PEHS the same rates as those ratepayers?**

625 A. Instead of charging PEHS the same higher rates that ratepayers were  
626 paying, the Companies recalculated the repair charges to its ratepayers at  
627 cost (Companies Ex. 2.0, 4-5) and then charged PEHS those same repair  
628 charges. (Companies Response to Staff DR DAS-1.02(e).)

629  
630 **Q. What was the result of the Companies re-calculation of ratepayer**  
631 **repair charges at cost and why is this result significant?**

632 A. Repairs charges to ratepayers dropped by more than half. While this is a  
633 positive development for ratepayers, it illustrates that the Companies had  
634 increased their charges for repair rates more than 2 times above costs,  
635 making the PPP offered by Companies' unregulated affiliate PEHS more  
636 attractive to ratepayers which were solicited by the call center reps.

637  
638 **Q. What is the history of these repair rates?**

639 A. The timing of repair charge increases appear to be targeted to make PPP  
640 more competitive, by making it cheaper relative to Company-provided  
641 repairs. Recall that the Companies had first notified Staff in March 2003 via  
642 email that they were planning to offer PPP as their own product. During that  
643 email, the Companies state that the repair rate is \$40 for the first 30

644 minutes.<sup>19</sup> (Attach. A, Email from A. Ikoma to J. Howard, March 24, 2003.)

645 The very next month, those repair rates were raised to \$60. By July 2005  
646 both Companies had reached the \$70 level. This remained in effect until  
647 January 2013. (Attach. G, Companies Response Staff DR DAS- 19.03.)

648

649 **Q. How did the Companies use their ratepayer repair rates to benefit**  
650 **PEHS?**

651 A. The Companies used this repair rate in its script where it states,

652 Now that we have your order completed Mr./Ms.\_\_\_\_\_,  
653 I'd like to offer you the Peoples Energy Protection Plus  
654 program which is offered through Peoples Energy Home  
655 Services, an affiliate of Peoples Gas.  
656 For only \$2.95 per month, repairs to inside leaks on your  
657 exposed pipes and appliance connectors will be covered at no  
658 charge for up to \$300. All work is guaranteed by this program.  
659 Without this coverage, repairs to inside gas leaks would cost a  
660 minimum of \$70 for the first ½-hour of service.  
661 'Would you be interested in enrolling?'

662

663 (Companies responses to Staff DR Docket Nos. 11-0280/0281  
664 (Cons.) DAS 2.09 and Att. 01.)  
665

666 **Q. Did the Companies deliberately increase charges to ratepayers above**  
667 **cost to benefit PEHS at ratepayers' expense?**

668 A. It is impossible to know if the Companies did this deliberately to help their  
669 affiliate while disadvantaging its ratepayers; however, it certainly had that

---

<sup>19</sup> Note that this is more than 30% above the 2012 cost-based rates. So the Companies were already profiting from these services.



670 effect. The Companies actions made the PPP more favorable to Company-  
671 provided repairs services than it would have been otherwise.

672

673 **Q. How does this evidence settle the question about the margin in those**  
674 **\$70 charges?**

675 A. According to the Companies, repair charges for ratepayers included a  
676 “markup” for profit margin. (Docket No. 11-0280/0281 (Cons.), Staff Ex.  
677 18.0, Attachment H - Companies responses to Staff DR DAS 9.08.) Given  
678 the reduction in rates as a result of the new cost study, despite the  
679 Companies’ witness, Ms. Gregor’s estimate that the margin was between  
680 10-20% (Docket No. 11-0280/0281 (Cons.), Companies responses to Staff  
681 DR DAS 13.02), it appears that this margin was actually more than 100%  
682 (NS-PG Ex. 2.1).

683

684 **Q. What additional evidence is there, which has not been previously**  
685 **presented to the Commission, regarding discriminatory provision of**  
686 **repair services?**

687 A. Another issue that arises is the diminished repair services that ratepayers  
688 receive relative to PEHS. PEHS has no employees of its own; thus, all  
689 actions that it took were done either by its officers or utility employees  
690 acting on its behalf. As indicated in Ms. Kallas’ testimony, the Companies  
691 will only make non-PPP repairs in some cases:

Q. If a customer requires repairs to customer-owned piping and the customer does not purchase the PPP service, will the Utilities repair the piping?

A. If the customer requests, the Utilities provide this service in some cases, but the Utilities have no obligation to provide the service. Also, the customer may contract with others for the service.

(NS-PGL Ex. 1.0, 5.)

As explained further in Mr. Julian's testimony, the Companies will only make non-PPP repairs if the tech has the time and parts to make those repairs on the spot.

Q. If a customer asks the Utilities to repair customer-owned piping, what do the Utilities consider in determining whether to make the repair?

A. Before agreeing to make the repair, the Utilities consider the nature of the repair, such as the amount of time and material that would be required, as well as other workload requirements, to determine if resources are available to make the repair.

(NS-PGL Ex. 2.0, 4.)

**Q. How did the Companies respond when asked if limitations on repairs are the same for PPP as non-PPP customers?**

A. When asked if the limitations on repairs are the same for PPP as non-PPP customers, the Companies answered that there is a difference because, "[s]ervice to PPP customers is subject to a contract" (Companies Response to Staff DR DAS-2.03(a)) between the customer and PEHS, not between the Companies and PEHS (Companies Response to Staff DR DAS-3.03). According to the Companies, service orders to non-PPP ratepayers who

725 need those repairs are sometimes turned down by the techs. (NS-PGL Ex.  
726 1.0, 5.)

727

728 **Q. Did the PEHS use any contractors for any repairs?**

729 A. No. All repairs to PEHS customers' customer-owned piping were completed  
730 by utility employees. Contractors were not used. (Attach. H, Companies  
731 Response to Staff DR Docket Nos. 11-0280/0281 (Cons.) DAS-2.12.)

732

733 **Q. Does this indicate discrimination by the Companies?**

734 A. Yes. For all intents and purposes, the Companies were providing repair  
735 services to their affiliate, PEHS, that were superior to those provided to  
736 ratepayers that do not have PPP, and thus, discrimination occurred.<sup>20</sup>

737

738 **Q. Does the Act address discrimination?**

739 A. Yes. The Act sets forth broad requirements for utilities that would provide  
740 services under the Act. Section 8-101 of the Act delineates  
741 "nondiscrimination" as one of the "[d]uties of public utilities." 220 ILCS 5/8-  
742 101. "A public utility shall, upon reasonable notice, furnish to all persons

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<sup>20</sup> Not only did PEHS get a higher grade of service, they were charged half of what the Companies charged ratepayers for the exact same repairs. If PEHS received a higher grade of repair service relative to that provide for non-PPP customers then they should have paid a premium for this service. As it was, PEHS was charged only the FDC for a standard repairs service. It is ironic that the utilities charged a premium price to its ratepayers for the inferior service. The Commission already determined that the utility must charge the same price to its affiliate as it charges to its ratepayers in the 2011 rate case.

who may apply therefor and be reasonably entitled thereto, suitable facilities and service, without discrimination and without delay." Id. (emphasis added).

**Q. Does this discrimination by the Companies violate the Commission Rules?**

A. Yes. Section 550.20 of the Commission's Rules, titled Non-Discrimination, generally prohibits discrimination in a broad range of actions by utilities in their interactions with affiliated interests. 83 Ill. Adm. Code § 550.20. There are three categories of entities identified and defined in Section 550.10: utilities, affiliated interests and un-affiliated entities (i.e., everybody else). Section 550.20 states:

Gas utilities shall not provide affiliated interests or customers of affiliated interests preferential treatment or advantages relative to unaffiliated entities<sup>21</sup> or their customers in connection with services provided under tariffs on file with the Illinois Commerce Commission (Commission), including contracts filed under tariffs filed pursuant to Section 9-102.1 of the Act [220 ILCS 5/9-102.1]. This provision applies broadly to all aspects of service, including, but not limited to, responsiveness to requests for service, the availability of firm versus interruptible services, the imposition of special metering requirements, and all terms and conditions and charges specified in the tariff.

83 Ill. Adm. Code 550.20(a) (emphasis added).

---

<sup>21</sup> The Rules define an unaffiliated entity as "any entity other than either the gas utility or any of the gas utility's affiliated interests." Since an "entity" is "something that exists by itself," ratepayers are unaffiliated entities.

Furthermore, sub-section (d) states, "A utility shall process requests for similar services provided by the utility in the same manner and within the same time period for its affiliated interests or their customers as for unaffiliated entities." 83 Ill. Adm. Code 550.10(d) (emphasis added).

**Q. Did PEHS make a request for repair services under the ISA?**

A. Yes. The Companies processed a request for repair services from PEHS on an expedited or more concrete basis that are similar to the repair services that they provided for ratepayers. The Companies could not have provided any service under the ISA without first receiving a request from PEHS to perform repairs services and the Companies agreeing to do so.

1. Upon request made from time to time by any party to this Agreement (hereinafter referred to as the "requesting party") to any other party hereto' (hereinafter referred to as the "requested party"), said requested party agrees to perform, within a reasonable time of the request thereof, any of the following acts: .... provided, however, that the requested party shall be under no obligation to perform any of the foregoing acts if, in its individual judgment and discretion, the performance thereof would in any way impair the ability of said requested party to fully discharge its corporate functions, or any of its functions subject to regulation. (Attachment to the Companies Corrected Response to Staff DR Docket No. 12-0299 DAS-7.01(k), 2-3.)<sup>22</sup>

**Q. Did the Companies enter into any MOU or contract other than the ISA?**

---

<sup>22</sup> Note also that under this agreement the Companies had a right to refuse to provide any service.

796 A. No. The Companies that indicated that there was no MOU or contract  
797 between themselves and PEHS; rather they bound themselves voluntarily in  
798 a verbal agreement to provide expedited concrete repair services to PEHS.

799 No, North Shore and Peoples Gas were not obligated to  
800 provide services that Peoples Energy Home Services  
801 requested. No contract or MOU existed that created an  
802 obligation. The Services and Transfers Agreement allowed  
803 Peoples Energy Home Services to request a service from  
804 North Shore and Peoples Gas, and North Shore and Peoples  
805 Gas had the right to provide or refuse to provide the service.

806  
807 (Companies Response to Staff DR DAS-11.03(b).)<sup>23</sup>  
808

809 **Q. What was the effect of the discriminatory repair services coupled with**  
810 **the lower repair rates?**

811 A. When coupled with the higher charges to ratepayers for the same repairs,  
812 these two actions resulted in PEHS possessing a more attractive product  
813 relative to the utility-provided repair services. According to the Companies,  
814 less than 5% of service orders to non-PPP ratepayers who need those  
815 repairs are turned down by the techs. Id. As the Companies averaged  
816 11,000 repairs annually between 2005-2010, this could mean as many as  
817 550 customers annually were denied services that they would have received  
818 if they had purchased PPP from PEHS. Since PPP ran for 8.5 years, this  
819 could be as many as 4700 customers.

820

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<sup>23</sup> The reference to the STA is incorrect because it was not the agreement in effect at the time that the service was initiated. The agreement in effect, the ISA, was approved by the Commission in Docket No. 55071. It offered the same right to provide service. (Companies Response to DR DAS-14.11(d).)

821 **Q. Have the Companies agreed to provide ratepayers with cost-based**  
822 **repair rates going forward even now that it no longer performs these**  
823 **repairs for PEHS?**

824 A. Yes. "North Shore and Peoples Gas will continue to provide repair  
825 services to customers under the same terms described in Mr. Julian's  
826 direct testimony (lines 59-64)." (Companies Response to Staff DR DAS-  
827 2.02(g).)

828

829 **Q. Have you uncovered any other actions that are not in the public**  
830 **interest with respect to the services provided by the Companies and**  
831 **IBS to PEHS?**

832 A. Yes. Billing Rates were not raised from 2004 when they were set at \$0.40  
833 per bill. Postage rose four times between 2004 and 2009 for an 18% total  
834 increase. At no time did the Companies increase billing charges to PEHS.  
835 Once questions were raised about it in the 2011 rate case, the charges were  
836 finally raised back to cost-level at \$0.54 per bill; at that time the postage was  
837 69% of all charges. Subsequent to this increase, rates again rose 2% in  
838 2012. PEHS still paid the lower charge though September 2013.

839

840 **Q. Did the Companies and their affiliate, IBS, make any attempt to follow**  
841 **the Commission-approved AIAs regarding billing charges?**

842 A. No. Neither the Companies nor IBS made any effort to keep billing rates  
843 at cost, despite the Commission's requirements that reasonable cost be

paid by PEHS under the ISA and Fully Distributed Costs be included under the STA.

**Q. Did the Companies charge rates to rate payers reflect rising postage costs?**

A. Yes. In each rate case from 2007 to 2012, the Companies included the current postage in their Operating Costs and Revenue Requirement. Additionally, their future test years reflected pending postage increases. (Attach. I, Companies Response to Staff DR DAS-19.01(f) and Attachment.) Therefore, the Companies were quick to ensure that they were made whole for all rising postage rates with respect to their own ratepayers but did not treat their affiliate with the same concern nor did they ensure that their affiliate IBS was fully compensated by PEHS with respect to postage costs IBS incurred in serving PEHS. This ultimately led to higher billing charges to ratepayers as costs that should have been borne by PEHS were time and again shifted to the Companies.

**Table 4 – Billing Charges to PEHS**

Year	Billing Party	Charges to PEHS	Postage Increases Included in Charges to Ratepayers	Postage Increase Date
2004	Peoples Gas	At Cost		
2005	Peoples Gas	At Cost		
2006	Peoples Gas	Below Cost	07-0241/0242(c.)	8-Jan-06



2007	Peoples Gas	Below Cost	07-0241/0242(c.)	14-May-07
2008	IBS	Below Cost	09-0166/0167(c.)	12-May-08
2009	IBS	Below Cost	09-0166/0167(c.)	11-May-09
2010	IBS	Below Cost		
2011	IBS	At Cost	11-0280/0281(c.)	18-Apr-11
2012	IBS	Below Cost	11-0280/0281(c.)	22-Jan-12
2013	IBS	Below Cost	12-0511/0512(c.)	27-Jan-13

861

862 **2. Peoples Gas and enovate**

863 **Q. Are you aware of another occurrence of improper affiliate interaction**  
864 **involving the Companies?**

865 A. Yes. As part of the Commission review of the Peoples Gas' FY2001 gas  
866 costs in Docket No. 01-0707, the Commission found that that Peoples Gas  
867 inappropriately interacted with its affiliate, enovate, in such a manner that  
868 increased gas costs to PGA customers while funneling profits to the  
869 affiliate. As part of a settlement in Docket No. 01-0707, Peoples Gas  
870 agreed, among other things, to provide a \$100 million reimbursement to  
871 ratepayers. The Peoples Gas Light and Coke Co., ICC Final Order  
872 Docket No. 01-0707, 144 (March 18, 2006) ("2001 Reconciliation Case").  
873 Staff has no desire to re-litigate this case; however, there are parallels  
874 with other issues presented here and this information is to provide the  
875 Commission with some context.

876

877 **Q. Did the Commission summarize Peoples Gas' interactions with**  
878 **enovate?**

879 A. Yes. The Commission found that enovate was an affiliated interest, as  
880 defined by the Act. The Commission stated:

881  
882 Enron NA and PERC each formed a subsidiary for the  
883 purpose of owning interest in another limited liability company.  
884 Enron NA formed Enron Midwest, LLC ("Enron Midwest" or  
885 "Enron MW"); PERC formed Peoples Midwest, LLC ("Peoples  
886 Midwest"). (Staff Ex. 7.00 at 8). These two entities then formed  
887 enovate, LLC to facilitate a profit-sharing arrangement that  
888 gave PEC/PERC 50% of all of the profits Enron Midwest  
889 gleaned through various business dealings with PGL.  
890 When Enron Midwest transacted business with PGL during  
891 the time period in question, 50% of Enron Midwest's profits  
892 were credited to enovate. Thus PEC/PERC received that 50%  
893 of Enron Midwest's profits. (Staff Ex. 9.00 at 15-16; 7.00 at  
894 11). Enron Midwest was the managing partner of enovate  
895 because it possessed the skills, resources and expertise to  
896 operate enovate efficiently and profitably. (Tr. 812-13).

897  
898 2001 Reconciliation Case Final Order at 15.  
899

900 **Q. Did the Commission find Peoples Gas' interactions with enovate**  
901 **violated the Act?**

902 A. Yes. The Commission found Peoples Gas and enovate interacted outside  
903 an agreement approved by the Commission. PGL filed for Commission  
904 permission to enter into a contract with enovate on November 28, 2000 in  
905 Docket No. 00-0760, but then filed a Motion to Dismiss that proceeding on  
906 March 21, 2001, which was granted. 2001 Reconciliation Case Final Order  
907 at 16.

908

909 However, PGL continued to directly transact business with  
910 enovate. PGL also transacted business with enovate  
911 indirectly, through Enron NA/Enron Midwest. At no time did the  
912 Commission approve any affiliate interest agreement between  
913 PGL and enovate.

914 ...  
915 enovate further conducted other transactions with PGL  
916 through Enron Midwest. To reiterate, none of enovate's  
917 transactions with PGL were made with Commission approval  
918 of an affiliated interest contract.

919  
920 Id. (emphasis added).  
921

922 **Q. Did the Commission find that Peoples Gas acted improperly with**  
923 **enovate?**

924 A. Yes. The Commission determined that Peoples Gas interacted with its  
925 affiliate, enovate, improperly resulting in imprudent and unreasonable gas  
926 charges:

927 Peoples Gas Light and Coke Company had not acted  
928 reasonably and prudently in its purchases of natural gas and  
929 other activities that affected that amounts collected through  
930 Gas Charges in its fiscal year 2001;

931 . . .  
932 pursuant to the Settlement Agreement and Addendum, a  
933 refund of \$100 million is to be distributed in the manner set  
934 forth above as part of the consideration paid in global  
935 settlement of this docket, as well as I.C.C. Docket Nos. 01-  
936 0706, 02-0726, 02-0727, 03-0704, 03-0705, 04-0682, 04-  
937 0683.

938  
939 Id. at 144.  
940  
941

942 **Q. Do you think that Peoples Gas' interactions with enovate are relevant**  
943 **to this case?**

944 A. Yes. Peoples Gas misled the Commission regarding its interactions with  
945 enovate. In its previous Petition to the Commission, Peoples Gas  
946 asserted that its interactions with enovate would be proper:

947 9. All transactions with enovate would be at arms length.  
948 Peoples would keep records of all transactions for regulatory  
949 review.

950 10. The Master Contract will not interfere with Peoples'  
951 operation of its public utility business or with the performance  
952 of its duties to the public. Moreover, the Master Contract will  
953 allow Peoples to optimize its gas supply and capacity assets.  
954 Transactions which optimize Company assets will result in a  
955 positive revenue stream that will either be automatically flowed  
956 to customers through the operation of the Company's Rider 2,  
957 Gas Charge, or will operate to recover fixed costs.

958 11. The Master Contract is in the best interests of Peoples and  
959 the customers it serves. Accordingly, this Petition should be  
960 reasonably granted, and the public will be inconvenienced  
961 thereby.

962  
963 The Peoples Gas Light and Coke Co., ICC Docket No. 00-  
964 0760, Petition at 3 (emphasis added).  
965

966 **Q. Were the actions with enovate at arm's length?**

967 A. No. Despite its assertion that all interactions were to be at "arm's length,"  
968 the Commission found that Peoples Gas treated enovate and its affiliates  
969 with preferential treatment.

970

971 **B. Questionable interactions with CNG affiliates by Peoples Gas.**

972 **Q. In addition to these cases where the Commission has already found**  
973 **against the Companies, are there any other instances where Peoples**  
974 **Gas has interacted with its affiliates which the Commission has not**  
975 **been made aware?**

976 A. In addition to these two instances of improprieties with PEHS and enovate,  
977 which have resulted in Commission action, Peoples Gas has twice  
978 interacted with two Compressed Natural Gas (“CNG”) affiliates completely  
979 outside the Commission-approved AIAs.

980

981 **1. Peoples Gas and Pinnacle**

982 **Q. How did Staff become aware of the Companies interactions between**  
983 **the Companies and Pinnacle?**

984 A. The Companies filed a petition to allow them to enter into an AIA with its  
985 affiliate Integrys Transportation Fuels (“ITF”) in Docket No. 12-0299.<sup>24</sup> In  
986 that case the Companies indicated that Peoples Gas and Pinnacle, an ITF  
987 subsidiary, were currently interacting apart from any Commission approval  
988 to have Pinnacle build a CNG station on its Division Street facility. The  
989 proposed AIA would have allowed the Companies to sell any CNG station  
990 to ITF without direct Commission pre-approval.

991

992 **Q. How did you respond to the ITF AIA in that case?**

993 A. I recommended that the Commission not approve the ITF AIA, because it  
994 was not in the public interest to give greater freedom to interact with ITF.

---

<sup>24</sup> Integrys created its subsidiary, ITF, “in August 2011 to invest in transportation fuel business opportunities.” The Companies report that Integrys “acquired two CNG infrastructure businesses, one comprised of Trillium USA Company and Trillium USA, LLC and the other comprised of Pinnacle CNG Company and Pinnacle CNG Systems, LLC.” (NS-PGL Ex. 1.0, 3, Docket No. 12-0299.) These companies became subsidiaries of ITF. Thus, the Companies are affiliates of ITF and its subsidiaries, including Pinnacle. (Companies Response to DR Docket No. 12-0299 RWB 1.07.)

995 After I filed my direct testimony in that case, the Companies withdrew their  
996 Petition.

997

998 **Q. How did the Companies characterize the nature of the relationship**  
999 **between the Companies and Pinnacle in Docket No. 12-0299?**

1000 A. During that case, Ms. Renier claimed that Pinnacle and Peoples Gas  
1001 “entered into an agreement prior to Integrys’ acquisition of Pinnacle and  
1002 the other transportation fuels companies, *i.e.*, prior to Pinnacle becoming  
1003 an affiliate of Peoples Gas.” She also claimed that “Pinnacle and Peoples  
1004 Gas are currently performing under this arm’s length agreement.” Docket  
1005 No. 12-0299 NS-PGL Ex. 1.0, 3-4 (emphasis added). Furthermore, Mr.  
1006 Wyrick also emphasized that, “this agreement pre-dated Pinnacle’s  
1007 affiliation with Peoples Gas.” Docket No. 12-0299 NS-PGL Ex. 2.0, 3.

1008

1009 **Q. Do you agree with the characterization of the contract between**  
1010 **Pinnacle and Peoples was an “arm’s length agreement”?**

1011 A. No. A series of events in 2011 and several internal Company  
1012 documents<sup>25</sup> listed below cause me to doubt the claims that the Peoples  
1013 Gas-Pinnacle contract was arm’s length. Also, as shown above, the  
1014 Peoples Gas made the same claim when it proposed to interact with its  
1015 affiliate enovate.

1016

---

<sup>25</sup> These documents are attachments to the Companies Responses to DAS-10.12(i), 20.01(a), 23.03(c) and 26.04.

**Q. Please describe the series of events in 2011 that cause you to disagree with the “arm’s length” characterization.**

A. Integrys, the holding company of Peoples Gas, entered into non-disclosure agreements (“NDA”) on May 18, 2011 with Pinnacle and Trillium, another company involved in CNG filing stations, in preparation for a merger. (Attach. J, Companies Response to DR Docket No. 12-0299 DAS 1.01(c).) On May 25, 2011, Peoples Gas terminated its CNG Station construction negotiations with Clean Energy. (Attach. K, Attachment D4.3.10b to Companies Response to Staff DR DAS-24.02(a).) On June 9, 2011, Peoples sent an RFP for services for a CNG filing station to Pinnacle, Trillium, and a third independent company, Dual Fuel Systems. (Attach. J, Attachment 1 to Companies Response to DR Docket No. 12-0299 DAS 1.01(e).) Pinnacle and Peoples Gas signed a contract for the construction of the CNG filing station on August 30, 2011. (Attach. J, Docket No. 12-0299 Companies Response to DR DAS 1.01(a).) Two days later, on September 1, 2011, Integrys acquired Pinnacle and Trillium. (Attach. J, Companies Response to DR Docket No. 12-0299 DAS 1.01(b).)

**Table 5 – Timeline of the Peoples Gas - Pinnacle Issue**

Date	Event
May 13, 2009	Peoples Gas submits pre-approval request to GTI
May 18, 2011	Integrys entered into non-disclosure agreements with Pinnacle and Trillium

May 25, 2011	Peoples Gas terminates its CNG station construction negotiations with Clean Energy
June 3, 2011	IntegrYS entered into a Mutual Confidentiality Agreement with Pinnacle
June 9, 2011	Peoples sent an RFP for services for the construction of the CNG filling station
August 30, 2011	Pinnacle and Peoples Gas signed a contract for the construction of the CNG filling station
September 1, 2011	IntegrYS acquired Pinnacle and Trillium
September 13, 2011	Schedule of Work from Pinnacle received by Peoples Gas
September 21, 2011	Peoples Gas and GTI enter into grant agreement
November 22, 2011	CNG Station construction begins
November 23, 2011	Peoples Gas requests 60-day extension
December 20, 2011	GTI imposed in-service deadline
April 6, 2012	CNG Station operation begins
September 14, 2012	Peoples Gas received \$163,000 credit from Pinnacle
December 18, 2012	Peoples Gas ask for full rate base amount

1036

1037 **Q. Please describe your understanding of the evolution of the**  
1038 **relationship between Peoples Gas and Pinnacle.**

1039 **A** I see three distinct periods in the relationship between Peoples Gas and  
1040 Pinnacle. First, there is the period of time before IntegrYS entered into



negotiation to acquire Pinnacle and Trillium in which these firms were unrelated. The second period was during those negotiations in which these firms were what I would label as “pending-affiliates.” The final (and current) period is the period as affiliates since the acquisition was complete.

**Q. What is it about this chain of events that causes you to reject the “arm’s length agreement” claim?**

A. Peoples Gas entered into a contract with a company that its parent company would acquire within just two days. All the negotiations with Pinnacle regarding the Pinnacle Agreement were completed after the NDA was signed – after Pinnacle and Peoples Gas were “pending affiliates.” In my opinion, it is not plausible that the pending affiliation had no effect on the timing and process of selecting Pinnacle to construct the CNG station. Additionally, all work performed by Pinnacle, all payments made by Peoples Gas and all change order approvals were made after the two firms were affiliates. Finally, as outlined below, several Peoples Gas internal documents reveal that there was affiliation influence on the interactions between Peoples Gas and Pinnacle both before and after they became affiliates.

1062 **Q. Was there any benefit to Integrys as a result of the timing of the**  
1063 **execution of the agreement between Peoples Gas and Pinnacle prior**  
1064 **to the finalization of the merger with Pinnacle?**

1065 A. Yes. If the merger was finalized first, then under the Act, the Peoples  
1066 Gas–Pinnacle contract would have required either Commission approval  
1067 for such an agreement or provision of the services at cost to Pinnacle  
1068 under the STA. 220 ILCS 5/7-101(3).

1069  
1070 **Q. Has the service contract for the CNG filling station been at issue in**  
1071 **any other cases before the Commission?**

1072 A. Yes. In the Companies 2012 Rate Case, Peoples Gas attempted to add  
1073 the CNG station to its rate base. Staff witness Seagle and I objected,  
1074 arguing that the costs had not been prudently incurred. See Staff Exs.  
1075 6.0, 31-36; 16.0, 13; 21.0 ibid., The Peoples Gas Light and Coke Co. and  
1076 North Shore Gas Co., ICC Docket Nos. 12-0512/0511 (Cons.) (“2012 Rate  
1077 Case”). Peoples Gas eventually withdrew the CNG station from its rate  
1078 base proposal. See Companies Ex. 44.0, 2, 2012 Rate Case. Much of the  
1079 evidence Staff presented in that case is relevant here because it shows  
1080 that Peoples Gas favored its then-pending affiliate, Pinnacle, in its  
1081 Request for Proposals (“RFP”) process, as I will discuss further below.

1082  
1083 **Q. Do you have other concerns about the contracting process followed**  
1084 **for the CNG fueling station contract?**

1085 A. Yes. The RFP process appears to have been conducted in a manner to  
1086 favor Pinnacle. The RFP was narrowly circulated to two of the  
1087 Companies' "pending affiliates" (one of which did not respond to the RFP)  
1088 and one independent firm, Dual Fuels Systems. Dual Fuels Systems did  
1089 not normally perform one of the services required in the RFP, and its lack  
1090 of response concerning that service resulted in the bid's rejection. In  
1091 addition, the response period allowed was quite short, which could have  
1092 contributed to the incomplete response by the independent bidder.

1093

1094 **Q. Did Peoples Gas allow sufficient time for the RFP response?**

1095 A. No. Peoples Gas set the RFP response date for June 22, 2011, which  
1096 allowed 13 days for the RFP response. (Attach. J, Attachment to  
1097 Companies Response Staff DR DAS-1.01(e).) Pinnacle submitted its bid  
1098 on Friday, June 24, 2011. Dual Fuel Systems submitted its bid on  
1099 Monday, June 27, 2011. (Companies Response to Staff DR Docket No.  
1100 12-0299 DAS-2.01.)

1101

1102 **Q. Has Peoples Gas defended the legitimacy of the contract bidding**  
1103 **process?**

1104 A. Yes. In the 2012 Rate Case, Peoples Gas witness Mr. Hoops stated that,  
1105 "[t]his project was competitively bid and bids were received from two  
1106 vendors." See NS-PGL Ex. 28.0, 11, 2012 Rate Case. Peoples Gas  
1107 maintained that its interactions with Pinnacle before its acquisition were at

1108 arms-length. “[T]he construction agreement was entered into by two  
1109 unrelated, unaffiliated companies under an arms-length agreement.”  
1110 (Companies Response to Staff DR DAS-9.02(c), 2012 Rate Case.)

1111

1112 **Q. How do you respond to Mr. Hoops’ statement?**

1113 A. The fact that Peoples ultimately received two bids, only one of which was  
1114 complete, does not show that the RFP was competitive. On the contrary,  
1115 the fact that Peoples Gas only received two bids is consistent with the  
1116 process not being competitive.

1117

1118 **Q. How else did Mr. Hoops defend the solicitation process?**

1119 A. Mr. Hoops claimed “Peoples Gas followed all business processes as with  
1120 any other project in bidding for this project.” (NS-PGL Ex. 28.0, 11, 2012  
1121 Rate Case.)

1122

1123 **Q. What is your response to this claim?**

1124 A. This statement was misleading because it suggests that People Gas  
1125 followed a set procedure for developing the list of recipients for its RFPs –  
1126 also known as a “bid list.” However, Peoples Gas admitted that “[t]here are  
1127 no documented procedural steps used during the creation of the bid list.”  
1128 (Peoples Gas’ response to Companies Response to Staff DR DAS 8.02(a),  
1129 2012 Rate Case.) Furthermore, an internal audit Summary Memo found  
1130 that there were inconsistencies between the standard practices and what

1131 actually occurred. (Attach. L, Attachment to the Companies Response to  
1132 Staff DR DAS-20.01(f).) This Summary Memo concluded that there needed  
1133 to be re-training because Peoples Gas did not follow procedures. Id.  
1134 However, Peoples Gas cannot have “followed standard business practices”  
1135 and failed to include Supply Chain services early in the process which  
1136 resulted in “appropriate procurement policies...not being utilized.” Id.

1137

1138 **Q. How did Peoples Gas determine the list of recipients for its RFPs?**

1139 A. Peoples Gas provided a “bid list” of firms to IBS Supply Chain Services<sup>26</sup>  
1140 to send the RFP. However, for the CNG station RFP process, that bid list  
1141 included only three firms. (Peoples Gas’ Response to DR DAS-8.02, 2012  
1142 Rate Case.) The bid list was compiled by a group of four individuals; the  
1143 group never considered any additional firms. It also did not conduct an  
1144 internet search to find other qualified firms. (Peoples Gas Response to  
1145 DR DAS-11.01, 2012 Rate Case.) Rather, Peoples Gas used only three  
1146 firms with which it had prior involvement and two of which it was acquiring.

1147

1148 **Q. How does Peoples Gas attempt to justify that its bid list selection**  
1149 **process was fair?**

1150 A. Peoples Gas insists that the people on the bid list group did not know  
1151 about the acquisition. (Attach. M, Companies Response to Staff DR DAS-  
1152 14.09(c).)

---

<sup>26</sup> IBS Supply Chain Services is a division within IBS that handles procurement.

1153 **Q. How do you respond to this claim by Peoples Gas?**

1154 A. I disagree with it. While Companies also insisted that the RFP process was  
1155 competitive (Peoples Gas Ex. 28.0, 11, 2012 Rate Case) and followed  
1156 standard business processes (Companies Response to DR ENG-6.05, 2012  
1157 Rate Case), I have learned that the senior member of the bid list  
1158 development group was Mr. Calvin (Peoples Gas' Response to DR DAS-  
1159 8.02, 2012 Rate Case.), a vice president who was privy to the acquisition  
1160 information (Attach. N, Revised Attachment 1 to the Companies  
1161 Supplemental Response to Staff DR DAS-10.19). Mr. Calvin approved the  
1162 bid list. (Attach. O, DAS-15.02(d).) Notably, Mr. Calvin also became an  
1163 employee of ITF and an officer of the winning firm (Companies Response to  
1164 Staff DR DAS-8.02, 2012 Rate Case.) BEGIN CONF. \*\*\*XXX  
1165 XXXXXXXXXXXXXXXXXXXXXXXXXXXX at his new employer. \*\*\* END CONF  
1166 (CONFIDENTIAL Attach. P, Companies Confidential Response to Staff DR  
1167 DAS-10.18.)

1168

1169 **Q. How else does Peoples Gas attempt to justify that its interaction with**  
1170 **Pinnacle was not preferential to Pinnacle relative to DFS?**

1171 A. Peoples Gas insists that the construction contract approval group were not  
1172 aware of nor influenced by the acquisition. (Attach. Q, Companies  
1173 Response to Staff DR DAS-7.02(f), 2012 Rate Case.)

1174

1175 **Q. How do you respond to this claim by Peoples Gas?**

1176 A. Integrys Audit Services conducted an audit that specifically looked at the  
1177 interactions between Pinnacle and Peoples Gas regarding the CNG  
1178 station construction contract. This audit evaluated whether there was any  
1179 preferential treatment in the RFP selection process and concluded that  
1180 there was no preferential treatment. (Attach. R, Attachment to the  
1181 Companies Response to Staff DR DAS-23.03(c), 2.)  
1182

1183 **Q. How do you respond to this audits conclusion?**

1184 A. Despite the finding in the audit report of many inconsistencies between  
1185 standard practice and this particular RFP selection process, the report  
1186 included only one reason why there was no preferential treatment, but  
1187 included three reasons to suggest preferential treatment in the selection  
1188 process. (Attach. R, Attachment to the Companies Response to Staff DR  
1189 DAS-23.03(c), 2-3.) The sole basis provided for the finding of no  
1190 preferential treatment was that all employees interviewed, save one Mr.  
1191 Walsh, “asserted no knowledge of the plans to acquire Pinnacle.” This  
1192 audit listed Mr. Calvin as one of those interviewed. (Attach. R, Attachment  
1193 to the Companies Response to Staff DR DAS-23.03(c), 2-3.) The  
1194 Companies now acknowledge, however, that Mr. Calvin, who approved  
1195 the bid list (Attach. O, Companies Response to Staff DR DAS-15.02(d)),  
1196 was also on the acquisition access list (Attach. S, Companies Response  
1197 to Staff DR DAS-10.19) and Mr. Calvin had knowledge at the time.  
1198 (Attach. T, Companies supplemental response to Staff DR DAS-18.01, p.

9) Thus, the conclusion of the report – that there was no preferential treatment - was based on information that was entirely incorrect.

**Q. What evidence in the report is inconsistent with the conclusion that there was no preferential treatment?**

A. The audit report makes note of several instances where Pinnacle was given preferential treatment. The audit makes the following statements:

- “Cost analysis did not reflect the \$100,000 (later changed to \$88,000 in Pinnacle’s revised proposal) proposed by Pinnacle for security work. The cost analysis used the competing bidder’s amount of \$36,500 [for security work].” (Attach. R, Attachment to the Companies Response to Staff DR DAS-23.03(c), 2-3.) The effect of performing the cost analysis in this manner made Pinnacle’s bid appear less costly than it really was. Pinnacle was paid the full price after the contract was won.
- “Pinnacle’s proposal amount was adjusted upwards to reflect the pricing of the competing bidder where Pinnacle did not (could not) include an amount for specific line items. After Pinnacle’s amount was adjusted upward, it exceeded the competing bidder’s proposal amount.” (Attach. R, Attachment to the Companies Response to Staff DR DAS-23.03(c), 2-3.) Thus, Pinnacle was not the cheapest bid, yet it won the contract.



1221                   • “There is no documentation to support that the competing bidder  
1222                   was allowed to counter.” (Attach. R, Attachment to the Companies  
1223                   Response to Staff DR DAS-23.03(c), 2-3.) Thus, Dual Fuels  
1224                   System appeared to be at a disadvantage here because it was not  
1225                   allowed to make a counter offer.

1226

1227   **Q.    What other evidence did you find that shows that Pinnacle received**  
1228           **preferential treatment from Peoples Gas and IBS?**

1229   A.    IBS entered into a Mutual Confidentiality Agreement (“MCA”) with Pinnacle  
1230           as part of this RFP process. This MCA became part of the construction  
1231           contract between Pinnacle and Peoples Gas. However, the MCA was not  
1232           signed on August 30, 2011 with the rest of the construction contract. Rather,  
1233           it was signed on June 3, 2011 before the RFP was sent out. (Confidential  
1234           Attach. U, Companies Response to Staff DR Docket No. 12-0299 RWB-1.03  
1235           and Confidential Attachment 4) Furthermore, neither Peoples Gas nor IBS  
1236           entered into any MCA with Trillium or Dual Fuel Systems. (Companies  
1237           Responses to Staff DRs DAS-25.02, DAS-27.01.) This indicates a  
1238           preference for Pinnacle before the RFP was even sent out.

1239

1240   **Q.    You indicate that one vendor did not provide a complete bid. Would**  
1241           **you elaborate on this point?**

1242   A.    Yes. Dual Fuel Systems, the independent vendor, did not provide a bid on  
1243           the operation and maintenance for the facility, which the RFP required.

1244 (NS-PGL Ex. 28.0 Rev., 11, 2012 Rate Case.) The RFP required a  
1245 proposal for operations and maintenance support, including all planned  
1246 and unplanned maintenance and repair, 24-hour monitoring and fault  
1247 detection, and the ability to remotely assist fueling customers. (Peoples  
1248 Gas' Response to DR 2012 Rate Case DAS-11.01, Attachment 1, 14-15.)  
1249 On January 15, 2013, Mr. Eric Schwab, the CEO and General Manager of  
1250 Dual Fuels Systems, indicated in a telephone conversation with me that  
1251 Dual Fuels Systems does not provide 24-hour monitoring and fault  
1252 detection or the ability to remotely assist fueling customers.  
1253

1254 **Q. Was there a need to include operations and support services in the**  
1255 **RFP?**

1256 A. I do not believe there was a legitimate need. Peoples Gas could have had  
1257 a separate RFP process for the operation and maintenance of its station,  
1258 allowing additional entities to submit bids for other aspects of the RFP.  
1259 My belief is supported by the fact that the winning bidder, Pinnacle, never  
1260 operated the station, therefore, there was no legitimate reason to  
1261 disqualify Dual Fuel Systems from consideration for not providing a bid for  
1262 a part of the RFP that the winning bidder was never called on to perform.  
1263 Additionally, Pinnacle also provided a bid that was incomplete in that it did  
1264 not provide cost estimates for all listed services. (Attach. V, Peoples Gas'  
1265 Response to DR DAS-11.04, Attachment 01, 2012 Rate Case.) As  
1266 Peoples Gas witness Mr. Wyrick indicated, "[t]he agreement [for which

there was the RFP was] for the construction of a fueling station. The agreement covered the construction of the station only and not operations.” NS-PGL Ex. 2.0, 3, Docket No. 12-0299.) ITF now operates the station. (Companies’ response to DR Docket No. 12-0299 DAS-1.02.)

**Q. What other factors may have influenced the selection of the bid?**

A. An internal document regarding the RFP Award Analysis Procedures of IBS Supply Chain Services, which conducts the RFP process, states that

BEGIN CONF. XXX

XX

XX

XXXXXXXXXX” \*\*\* END CONF (Confidential Attach. W, Peoples Gas’

Response to DR DAS-10.01, Confidential Attachment 04, 1-2, 2012 Rate

Case (emphasis added).) BEGIN CONF XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX

XX

XX

XXXXXXXXXXXXX END CONF

**Q. Were there any other factors that may have influenced the RFP process?**

A. Yes. Peoples Gas pursued and received a grant from the City of Chicago (“City”) to build the CNG station. In May 2009, Peoples Gas submitted for pre-approval of its grant with the City. At that time, Peoples Gas

estimated that the cost of the station would be \$692,400, and it asked for funding of the entire amount. (Peoples Gas' Response to Staff DR DAS-7.01, Attachment 01, 4, 2012 Rate Case.) Peoples Gas eventually signed a grant agreement that dictated the terms and conditions under which the grant funds would be provided to Peoples Gas. (Peoples Gas' Response to DR ENG-6.02 Attachment 01, 2012 Rate Case.) The fact that Peoples Gas thought it would get the station without spending any of its own money may have induced it to move ahead. However, its initial estimate was severely understated. The total project costs rose to \$1,550,092.<sup>27</sup>

**Q. Did Peoples Gas have a compressed time-line that would preclude a second, longer RFP process or a second RFP with a broader dispersion once it received only one complete bid?**

A. No. The stated project completion date was December 20, 2011. (Attach. J, Attachment to Companies Response to Staff DR Docket No. 12-0299 DAS-1.01(e), 1.) However, when Peoples Gas entered into the contract with Gas Technology Institute ("GTI"), it had already received a progress schedule from Pinnacle that reflected that the station would not be operational until late January. (Attach. X, Companies Response Staff DR DAS-25.02(a).) Thus, Peoples Gas knew that it would not be able to fulfill this obligation. Additionally, construction on the CNG station did not begin until November 22, 2011. (Companies Response to DR Docket No. 12-

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<sup>27</sup> Rate base amount \$857,692 plus grant amount \$692,400. (Peoples Gas Response to Staff DR DAS-6.02(f) 2012 Rate Case.)

0299 DAS-1.01(f).) The station was not functionally operational until April, 6 2012. (Companies' Response to DR Docket No. 12-0299 RWB-1.05(c).) Furthermore, Peoples Gas states that: "[t]he station construction RFP date was set by the project group with the goal of meeting or exceeding the in service requirements set forth in the grant agreement. The grant agreement did not preclude the requirement of any selected vendor to meet an earlier work completion date." (Peoples Gas Response to DR DAS-7.02, 2012 Rate Case.) On November 23, 2011 Peoples Gas proposed to GTI to extend the deadline by 60 days, indicating that it had been in discussions with GTI and found GTI open to such an extension. (Attach. Y, Companies Response to Staff DR DAS-26.02 and Attachment.) This extension was not formally accepted (Attach. Y, Companies Response to Staff DR DAS-26.02(b)), but Peoples Gas was never penalized by GTI for not completing the station before December 20, 2011 (Companies Response Staff DR DAS-22.01(g)). It is worth noting that Peoples Gas had been considering this project for more than two years before it sent out its RFP. There was ample time for it to find other qualified firms. The compressed RFP timeline could have been influenced and rushed by the impending acquisition of Pinnacle and the additional affiliate contracting requirements that affiliation would cause.

**Q. What do you conclude about the RFP process?**

1334 A. Competitive pressures on Pinnacle were removed by sending the RFPs to  
1335 two pending affiliates and only one independent company that did not  
1336 provide all the “required” services. Peoples Gas failed to conduct any  
1337 research to find any other possible firms outside of those already known to  
1338 it. A good faith effort to have a competitive RFP process would have  
1339 required a broader solicitation with more time to respond.

1340

1341 **Q. Could the affiliate status of Pinnacle affect its bid and subsequent**  
1342 **selection by Peoples Gas?**

1343 A. Yes. It would be reasonable for Pinnacle to have had an expectation that  
1344 when it submitted its bid, it would be an affiliate of Peoples Gas before it  
1345 began construction, which, in fact, is precisely what occurred. Therefore,  
1346 Pinnacle may have been able to offer a lower bid with some expectation  
1347 that, despite language in the contract indicating the bidder would be  
1348 responsible for cost over-runs, Peoples Gas might not hold it responsible  
1349 for cost over-runs or other financial penalties that might arise. The initial  
1350 bid submitted by Pinnacle was \$888,775. (Companies Response to DR  
1351 Docket No. 12-0299 DAS-1.01(g).) The total amount that Peoples Gas  
1352 paid to Pinnacle was \$1,375,208.95. (Attach. Z, Attachment 1 to  
1353 Companies Response to Staff DR DAS-22.02. Thus, the amount paid to  
1354 Pinnacle rose more than 54% above the price of the bid. Peoples Gas  
1355 proposed in its rate case to include the increase in the amount paid to  
1356 Pinnacle in rate base in that proceeding, with no cost overruns absorbed

1357 by Pinnacle. Also, when it selected its “pending affiliate” Pinnacle as the  
1358 winning bidder, Peoples Gas was reasonably certain that Pinnacle would  
1359 be an affiliate *before any work commenced*. Indeed, affiliation occurred  
1360 two days after the contract was signed.

1361

1362 **Q. What did the Companies state regarding the connection of the**  
1363 **Construction contract process and the acquisition of Pinnacle?**

1364 A. The Companies insist that there was no rush to get the contract approved  
1365 before the acquisition was executed. (Attach. AA, Companies Response  
1366 to Staff DR Docket No. 12-0299 DAS-7.02(g).) They also insist that  
1367 neither they nor their affiliates expedited the approval of this contract to  
1368 allow the acquisition to occur.<sup>28</sup> (Attach. AB, Companies Supplemental  
1369 Response to Staff DR DAS-18.03(a).)

1370

1371 **Q. Were the two processes connected?**

1372 A. Yes. The Project Change Request along with the attached email string  
1373 brings the involvement of Mark Radtke into focus. Mr. Radtke was the  
1374 project sponsor, and authorized the payment of the change order requested  
1375 by Pinnacle through Jeff Krueger, one of the co-project managers along with  
1376 Mr. Wyrick. (Attach. AC, Attachment 2 to the third supplemental response to  
1377 Staff DR DAS-10.12) This form included the description of the project and

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<sup>28</sup> Rather, they claim that “Efforts to complete the RFP process were in response to the upcoming deadline set forth in the grant agreement. (Companies Response to Staff DR DAS-18.03(a).) However, the grant agreement between GTI and Peoples Gas was not even signed and the deadline on the grant agreement between the City and GTI was for 21 Dec 2012, more than 15 months distant.

the Change Orders to be approved. “This project was for EPC services from Pinnacle CNG to Peoples Gas for the installation of a CNG filling station. During the course of contract negotiations, several scoped line items were un-priced by Pinnacle. In an effort to expedite the purchase of Pinnacle CNG by Integrys Energy Group, a final price was not determined for un-priced line items, instead an "allowance" was made for the unpriced line items. Id. (emphasis added). Mr. Radtke approved this Project Change Request after stating “we [PGL] were not disputing the legitimacy of the charges, even though we did not anticipate they would be so large.” Thus, the acquisition process was not only connected to the construction project, the acquisition was dependent upon the construction process approval and there was pressure to get the construction project approved rapidly so that the acquisition could go through. The award group, which included Mr. Radtke, the project sponsor, and Mr. Krueger, one of the project managers, knew that the two processes were linked. (Attach AD, Attachment to Companies Response Staff DR DAS-26.04.)

**Q. What did the Companies state regarding Mr. Radtke’s and Mr. Krueger’s foreknowledge of the acquisition?**

A. The Companies stated that Mr. Radtke “was not involved in the station transaction negotiations with Pinnacle although he was involved in prior matters related to the grant and prior contract matters associated with the station. These events, and his awareness of the events that led to the



1401 CNG station at Division Street, occurred in 2010 and 2011. He does not  
1402 recall specific dates when he became aware of the contract award to  
1403 Pinnacle.” They also state that Mr. Krueger “became aware of the  
1404 acquisition when it was announced (the company press release is dated  
1405 September 1, 2011).” (Attach. T, Companies Supplemental Response  
1406 Staff DR DAS-18.01) As the Project Change Request Form shows, both  
1407 of these individuals knew that the construction and acquisition processes  
1408 were linked, that the construction contract process has been expedited  
1409 and that corners had been cut to get the construction contract signed  
1410 before acquisition. (Attach AD, Attachment to Companies Response Staff  
1411 DR DAS-26.04.)

1412

1413 **Q. In the 2012 Rate Case, Mr. Hoops testified in part as follows**  
1414 **regarding the selection of Pinnacle as the winning bidder:**

1415 **This project was competitively bid and bids were received**  
1416 **from two vendors. However, the bid from one vendor was not**  
1417 **complete as it did not provide for the required operation and**  
1418 **maintenance support of the installed product. The other bid**  
1419 **was complete and was otherwise satisfactory. Therefore, the**  
1420 **selected vendor was based on the only complete bid. The fact**  
1421 **that the company that was selected, then became an affiliate,**  
1422 **does not change these facts**

1423

1424 **(NS-PGL Ex. 28.0 Rev, 11, 2012 Rate Case.) Do you have any**  
1425 **comment with respect to enforcement of terms of the contract to**  
1426 **include cost over-runs?**

1427 **A. Yes, The agreement between Peoples Gas and Pinnacle has been**  
1428 **described as an “arms length agreement.” (NS-PGL Ex. 1.0, 3-4 Docket**

No. 12-0299.) However, I find this to be misleading on many fronts,  
including the enforcement of terms of the contract. Peoples Gas states:

[T]he construction agreement was entered into by two  
unrelated, unaffiliated companies under an arms-length  
agreement. The indemnification terms just like the other terms  
are not only standard for Peoples Gas but are also at least as  
protective to Peoples Gas as one would find elsewhere in the  
market. The terms of the agreement speak for themselves and  
are fully-enforceable by both parties just as they would be if  
the agreement had been entered into between Peoples Gas  
and an entity that became an affiliate five years after signing  
the agreement or if Peoples Gas had entered an agreement  
with another unaffiliated contractor that Peoples Gas  
considered for the work such as Dual Fuels.

(Peoples Gas' Response to Staff DR 2012 Rate Case  
(emphasis added).)

All work performed under the contract was performed by Pinnacle while it  
was an affiliate with Peoples Gas. All payments to Pinnacle were made  
after it was an affiliate. (Attach. Z, Attachment 01 to the Companies  
Response to Staff DR DAS-22.02.) Any cost over-runs or change orders  
would have to be negotiated by both firms as affiliates. (Companies'  
response to DR Docket No. 12-0299 DAS 1.04.) If the performing party  
had been the unaffiliated Dual Fuel Systems, then Peoples Gas would  
have had an economic incentive to not allow Dual Fuel Systems to pass  
along those added costs to the Company. Because Pinnacle was already  
an unregulated affiliate, however, passing along additional costs and  
negotiating for change orders might allow the Utility to pass those costs on  
to ratepayers and shield Integrys its affiliate from such costs. I similarly

1459 testified that the affiliate relationship could lead to cost overruns in the  
1460 2012 rate case. (Staff Ex. 21.0, 23-24, 2012 Rate Case.)

1461

1462 **Q. What other evidence did you find about Peoples Gas' treatment of**  
1463 **cost overruns?**

1464 A. The change order approval email demonstrates that Peoples Gas  
1465 approved all change orders at the exact price and contractor margin that  
1466 Pinnacle requested. While the Companies insisted that the 15%  
1467 contractor margin was a part of the contract (Attach. AC, Companies Third  
1468 Supplemental Response to Staff DR DAS-10.12(i)), the contract does not  
1469 specify any margin and both Pinnacle and Peoples Gas were aware that  
1470 no margin was specified, as evidenced by Pinnacle's mention of this fact  
1471 to Peoples Gas in the change order request (Attach. AE, Attachment 1 to  
1472 the Companies Response to Staff DR DAS-18.02). After review by  
1473 Integrys accounting (which followed Staff's inquiry into this transaction),  
1474 Pinnacle was forced to refund \$163,723 to Peoples Gas more than half of  
1475 its cost overruns. (Attach. R, Attachment to Companies Response to Staff  
1476 DR DAS-23.03(c).) Evidence shows that the cost over-runs were due in  
1477 part to Pinnacle overcharges to Peoples Gas. (Attach. AF, Supplemental  
1478 Companies Response to Staff DR DAS-23.01c and Attachment)

1479

1480 **Q. Did Peoples Gas' notify the Commission or Staff of this refund?**

1481 A. Peoples Gas neither testified about nor alerted the Commission or Staff to  
1482 this adjustment in either the 2012 Rate Case or Docket No. 12-0299. Nor  
1483 did Peoples Gas adjust its proposed rate base addition down to reflect the  
1484 lower cost actually incurred (Attach. AG, Companies Response to Staff  
1485 DR DAS-21.04(e)), despite the fact that it received the refund on  
1486 September 27, 2012. On the contrary, Peoples Gas still insisted that the  
1487 full project amount had been prudently incurred and attempted to (over-  
1488 )recover more than the full amount of the project. Taxpayers had already  
1489 paid \$692,400 (received in June 2012) and the Peoples Gas sought to  
1490 recover \$857,692 from its ratepayers for a total amount of \$1,550,092,  
1491 despite the fact that Peoples Gas knew before it filed rebuttal testimony on  
1492 December 18, 2012 that it had only spent \$1,408,021.83. Peoples Gas  
1493 should have reduced its proposed rate base amount by the amount of the  
1494 credit and acknowledged that it had overpaid Pinnacle.

1495

1496 **Q. How does the Companies' proposal to enter into an AIA with ITF in**  
1497 **Docket No. 12-0299 factor in here?**

1498 A. The Companies proposed to adopt an AIA with ITF in Docket No. 12-  
1499 0299. The only incremental service that would have been allowed under  
1500 the ITF AIA would have been for property transfers (sales). Peoples Gas  
1501 could have transferred the Pinnacle CNG station to ITF after it was  
1502 established and commercially viable without any Commission approval.

1503 Thus, it appears that the purpose all along with this station was for ITF to  
1504 end up with the station, but only if it was in the shareholders best interests.

1505

1506 **Q. Even though the Companies withdrew their ITF AIA petition, is the**  
1507 **issue of the sale of this station still relevant?**

1508 A. Yes. The Master AIA which went into effect after the withdrawal of the  
1509 Petition in Docket No. 12-0299 allows the Companies to sell property to  
1510 their affiliates without subsequent Commission approval regardless of the  
1511 amount. (Companies Response to Staff DR DAS-6.02a) Given that the  
1512 timing of any such a transfer will certainly occur when optimum for the  
1513 affiliate and the pricing of this transfer will be highly speculative, I do not  
1514 think that this transfer would be in the public interest. Regardless, the  
1515 Commission should review the precise details of any such property  
1516 transfer and determine if the deal is reasonable.

1517

1518 **Q. What do you conclude from the evidence provided here concerning**  
1519 **the record of actions by Peoples Gas in its relations with Pinnacle?**

1520 A. Peoples Gas' actions reflect favoritism toward its affiliate Pinnacle at the  
1521 expense of its customers and are not consistent with the public interest.

1522

1523 **Q. Is there any other aspect of the Pinnacle acquisition that concerns**  
1524 **you?**

1525 A. Yes. The Companies did not notify the Commission when ITF was added  
1526 to the STA. The STA requires that the Companies notify the Commission  
1527 when adding a party to the STA. According to Paragraph 2. Notices to  
1528 Article X REGULATORY REQUIREMENTS of the STA:

1529 Peoples Gas and North Shore shall notify the Commission  
1530 each time a new Party becomes eligible to receive or provide  
1531 Services and Facilities or transfer or acquire assets under this  
1532 Agreement.

1533 a. This notice shall be by means of a letter to the following or  
1534 any successor to the following: Commission's Manager of  
1535 Accounting, Manager of the Energy Department, Public  
1536 Utilities Bureau Chief, the Executive Director and an  
1537 informational filing in the Commission docket in which this  
1538 Agreement was approved.

1539 b. Such notice shall include: (i) a description of the anticipated  
1540 transactions between Peoples Gas or North Shore and the  
1541 new Party; (ii) a revised organizational chart showing all  
1542 Parties and their subsidiaries; (iii) a list of the Board of  
1543 Directors and officers of the new Party; (iv) a statement of  
1544 whether Peoples Gas and North Shore expect the new Party  
1545 to be a Providing Party, Receiving Party Transferring Party or  
1546 Acquiring Party; and (v) a statement regarding the expected  
1547 quantity of transactions that Peoples Gas or North Shore  
1548 expects to conduct with the new Party.

1549  
1550 (Companies Response Staff DR DAS-1.01(a) Attachment 1,  
1551 10.)

1552  
1553 Thus, the Companies failure to notify the Commission was not in  
1554 compliance with the STA.

1555

1556 **Q. How is this lack of notice affecting the issue of Commission relevant**  
1557 **here?**

1558 A. The failure to provide notice is an example of the Companies failing to  
1559 take appropriate actions regarding their interactions with their affiliates. If

1560 the Companies cannot follow the requirements of the AIA already in place,  
1561 the Commission should restrict them further.

1562

1563 **2. Peoples Gas and PNGV Corp.**

1564 **Q. Have you found other questionable interactions between Peoples**  
1565 **Gas and another of its CNG affiliates?**

1566 A. Yes. During the investigation into the facts surrounding the relationship  
1567 between Peoples Gas and Pinnacle, I found a reference to another CNG  
1568 station that pre-dated the current CNG station, this one “operated” by  
1569 PNGV Corp.. As I investigated further, I found evidence of disregard for  
1570 the terms of the AIA approved by the Commission.

1571

1572 **Q. Please give some background on the PNGV Corp. CNG station.**

1573 A. During 1995-1996, Peoples Gas built a CNG station on its Division Street  
1574 property for its affiliate PNGV Corp. to use. PNGV Corp. was added to the  
1575 ISA on January, 28, 1994. (Companies Response to Staff DR DAS-  
1576 14.05(e).) Since PNGV Corp. had no employees (Companies Response  
1577 to Staff DR Docket No. 12-0299 DAS-10.01(f)), Peoples Gas provided all  
1578 services needed to build and operate the station for PNGV Corp.  
1579 (Companies Revised Response to Staff DR Docket No. 12-0299 DAS-  
1580 11.04(c).) Peoples Gas constructed the station between December 1995  
1581 and June 1996 and spent more than \$479,000 on external costs for the  
1582 construction. (Attach. AH, Companies Response to Staff DR DAS-16.01.)

1583 In addition, Peoples Gas incurred internal labor costs as well as permitting  
1584 costs. (Companies Supplemental Responses to Staff DRs DAS-17.05(g),  
1585 (h).) Peoples Gas provided service to PNGV Corp. from April 1996-  
1586 September 16, 2003 under tariff S.C. No. 8 – Compressed Natural Gas  
1587 Service. PNGV Corp. “operated the station” using Peoples Gas  
1588 employees. (Companies Revised Response to Staff DR Docket No. 12-  
1589 0299 DAS-11.04(c).)

1590

1591 **Q. In addition to the tariffed S.C. No. 8 service, were there any non-**  
1592 **tariffed services Peoples Gas charge PNGV Corp. for?**

1593 A. Yes. Peoples Gas charged PNGV Corp. monthly for financing<sup>29</sup>  
1594 (Companies Response to Staff DR Docket No. 12-0299 DAS-10.02(t) (aka  
1595 “Rent Expense” or “Rental Expense”), supplies (Attach. A1, Attachment to  
1596 Companies Response to Staff DR Docket No. 12-0299 DAS-7.01(h) and  
1597 property management<sup>30</sup> (Companies Response to Staff DR Docket No.  
1598 12-0299 DAS-10.01(a).)

1599

1600 **Q. Under what authority did Peoples Gas provide these non-tariffed**  
1601 **services to PNGV Corp.?**

1602 A. Peoples Gas never entered into a specific agreement with PNGV Corp.  
1603 regarding this station. Rather, Peoples Gas provided these services

---

<sup>29</sup> Called “Rent Expense” by Peoples Gas. Attachment to Companies Response to Staff DR Docket No. 12-0299 DAS-7.01h

<sup>30</sup> Called “Labor Rebill” by Peoples Gas. Attachment to Companies Response to Staff DR Docket No. 12-0299 DAS-7.01h



1604 under the ISA which required that Peoples Gas recover from PNGV Corp.  
1605 all "Reasonable Costs," defined as "that amount of money which will make  
1606 the requested party whole for all costs and expenses relating to the  
1607 performance of such acts." <sup>31</sup> (Attachment to the Companies' Corrected  
1608 Response to DR DAS- 7.01(k).)

1609  
1610 **Q. How did Peoples Gas disregard its Commission-approved**  
1611 **agreement?**

1612 A. Peoples Gas never recovered the reasonable costs from PNGV Corp.  
1613 Therefore, Peoples Gas subsidized PNGV Corp and violated this  
1614 Commission-approved agreement.

1615  
1616 **Q. Was the "Rent Expense" that Peoples Gas billed PNGV Corp.**  
1617 **actually for Rent?**

1618 A. No. Peoples Gas indicated that "the yearly rental expense amount  
1619 represents only a return on investment for costs incurred by Peoples Gas  
1620 for construction of the station." (Peoples Gas Response to Staff DR  
1621 Docket No. 12-0299 DAS-10.02.) In fact, Peoples Gas provided detailed  
1622 information on what was included in the "Rent Expense" charge. (Attach.  
1623 AJ, Attachment to Companies Response to Staff DR Docket No. 12-0299

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<sup>31</sup> "The requested party shall charge the requesting party an amount equal to the reasonable cost of performing any of the acts requested and performed in the manner described in Paragraph 1 hereof. For purposes of this Agreement, the words "reasonable cost" shall mean that amount of money which will make the requested party whole for all costs and expenses relating to the performance of such acts." (Companies' Corrected Response to DR Docket No. 12-0299 DAS-7.01(k).)

1624 DAS-9.02.) That information is provided in Table 6 – Peoples Gas’ Rent  
1625 Expense Charges to PNGV Corp. set forth below:

1626 **Table 6 – Peoples Gas’ Rent Expense Charges to PNGV Corp.**

Station Facilities and Installation	\$172,607.45
Islands and Paving	\$114,146.13
Sidewalk	\$3,000.00
Security	\$21,875.89
Total Charges	\$311,629.47
Rate of Return-Per Dkt. # 95-0032	12.9180%
Yearly Rental Expense	\$40,256.29
Monthly Rental Expense	\$3,354.69

1627  
1628 All the inputs to the total charge are one-time, construction-related  
1629 charges to which a rate of return is applied to determine the so-called  
1630 “rental charge.” It’s a finance charge, and only on a portion of the capital  
1631 costs that Peoples Gas used for PNGV Corp.’s benefit.

1632

1633 **Q. Was this expansion of its utility plant for the exclusive benefit of**  
1634 **PNGV Corp. analogous to any other charges that Peoples Gas**  
1635 **charges?**

1636 **A.** Yes. Peoples Gas expanded its utility plant for PNGV Corp. in a manner  
1637 that benefitted only PNGV Corp as Peoples Gas never used this facility for  
1638 CNG purposes. (Supplemental Response to Staff DR DAS-17.05) This is

1639 analogous to main extensions, where the Utility expands its utility plant for  
1640 the exclusive benefit of a third party – prospective ratepayers. In that latter  
1641 case, Peoples Gas charges the third party up front for the maximum amount  
1642 allowed by the Commission's Rules for main extensions.<sup>32</sup> (Attach. AH,  
1643 Companies Supplemental Response to Staff DR DAS-11.01(a).) This  
1644 charge would include costs associated with parts, labor, overhead, permits  
1645 and loadings. (Attach. AL, Companies Response to Staff DR DAS-15.03i().)  
1646 An affiliate should not get a better deal than prospective ratepayers desiring  
1647 to expand utility plant for their own use.

1648

1649 **Q. How was this expansion of its utility plant for the exclusive benefit of**  
1650 **PNGV Corp. different from main extensions that Peoples Gas**  
1651 **performs for prospective ratepayers?**

1652 A. In a main extension, the prospective ratepayer is required to provide the  
1653 entire amount of capital up front before the project begins. Here, Peoples  
1654 Gas provided the capital for PNGV Corp., essentially loaning PNGV Corp.  
1655 the entire amount needed to construct this station.

1656

1657 **Q. Did PNGV Corp. pay for the reasonable financing and construction**  
1658 **costs associated with the CNG station?**

---

<sup>32</sup> There is a small amount of free extension either (100-200 feet). These charges are called deposits but are only refunded if another third party makes use of the new plant within 10 years; however, in the event of a refund, the utility is still made whole for all of its costs.

1659 A. No. Peoples Gas never charged PNGV Corp. for a single penny of the  
1660 construction cost. The only charge that Peoples Gas charged PNGV Corp.  
1661 for the project was a discounted finance charge based on 65% (Attach. AJ,  
1662 Docket No. 12-0299 DAS-9.02(a)) of the over \$479,964.42 in external  
1663 construction costs (Attach. AH, Companies Response to Staff DR DAS-  
1664 16.01). PNGV Corp. paid this discounted finance charge but never had to  
1665 pay back the principal. Rather, it only paid the interest on a portion of the  
1666 principle for 7 years, from 1996 to 2003. (Attachment to the Companies  
1667 Supplemental Response to Staff DR Docket No. 12-0299 DAS-7.01(h.)  
1668

1669 **Q. Did Peoples Gas recover its investment for the construction of the**  
1670 **station from PNGV Corp.?**

1671 A. No. By my conservative estimate, PNGV Corp. paid only \$278,439.27 in  
1672 rental expense to Peoples Gas between October 1996 and September  
1673 2003.<sup>33</sup> Thus, Peoples Gas spent more than \$311,629.47 in external  
1674 costs on this project, but never recovered any of those original  
1675 construction costs cost.  
1676

1677 **Q. Did Peoples Gas protect itself from any risk that PNGV Corp. might**  
1678 **go out of business before it paid for the reasonable financing and**  
1679 **construction costs associated with the CNG station?**

---

<sup>33</sup> To reach this total, I used the amount provided by Peoples Gas for the years which it had records (FYs 1997, 1999, 2001-2003) and used the same monthly rental expense (\$3354.69) for each month that was not provided (FY1998, 2000).

1680 A. No. Remarkably, Peoples Gas never entered into any sub-agreement or  
1681 memorandum of understanding requiring that PNGV Corp. remain in  
1682 business for any length of time or to pay back the principal on the loan. This  
1683 CNG market was very risky as it was an unproven technology. Peoples Gas  
1684 could have protected itself and its customers by requiring PNGV to sign a  
1685 lease of sufficient term to protect itself from the failure of PNGV Corp.'s risky  
1686 venture and charged enough monthly to repay the amount of the principle.  
1687 However, Peoples Gas could produce no Memorandum of Understanding  
1688 (Companies Response to Staff DR DAS-10.02(e)) and either had no  
1689 recourse to PNGV Corp. assets or made no claim on them when PNGV  
1690 Corp. ceased operations. Such a favorable arrangement, with no risk for  
1691 stranded capital investment for the tenant when the nascent market did not  
1692 develop, would not likely have been offered to an unaffiliated party.

1693

1694 **Q. What is your opinion of the agreement, given that Peoples failed to**  
1695 **protect itself from this risk?**

1696 A. The arrangement between PNGV Corp. was inappropriate. Peoples Gas  
1697 never should have entered into this type of arrangement without holding its  
1698 affiliate responsible until all costs were recovered. As it turned out, PNGV  
1699 Corp. closed shop before Peoples Gas recovered the construction costs,  
1700 much less a financing charge, for the CNG station. (Attach. AJ, Peoples Gas  
1701 Response to Staff DR Docket No. 12-0299 DAS 9.02 and Companies  
1702 Response to Staff DR Docket No. 12-0299 DAS 10.01.) PNGV Corp. left

1703 Peoples Gas with an asset that Peoples Gas had never used (Companies  
1704 Supplemental Response to Staff DR DAS-17.05) nor was it ever able to  
1705 “lease” the station again (Companies Response to Staff DR DAS- 10.02(g)).  
1706 If Peoples Gas had provided \$311,000 to PNGV Corp. at the beginning of  
1707 the project, and if PNGV Corp. had provided \$311,000 at the end of the 7  
1708 years, the finance charge would have been reasonable. However, PNGV  
1709 Corp. took cash at the beginning and returned a valueless asset at the end.  
1710 This is not a reasonable arrangement for Peoples Gas to enter into. It would  
1711 not have made a similar arrangement with a non-affiliate.

1712

1713 **Q. When you say that this charge was a discounted finance charge,**  
1714 **what do you mean?**

1715 A. Peoples Gas calculated the finance charge based upon \$311,000 which was  
1716 only a portion of its external costs. The total external costs without any  
1717 permitting were \$479,000; adding in permitting for the project would have  
1718 further increased costs. (Companies Supplemental Response to Staff DR  
1719 DAS-17.05(h).) Additionally, Peoples Gas never included any of its labor  
1720 and overhead costs associated with designing and managing the station  
1721 construction. (Companies Supplemental Response to Staff DR DAS-  
1722 17.05(g).) Thus, the finance charge was inadequate even to compensate for  
1723 the use of its capital for those 7 years.

1724

1725 **Q. Were there any other charges that Peoples Gas failed to charge**  
1726 **PNGV Corp.?**

1727 A. Yes. Peoples Gas never charged for compression of the natural gas that it  
1728 supplied during the 7 years that PNGV Corp. operated its CNG station.  
1729 (Companies Responses to Staff DRs DAS-14.07; 15.08.)

1730

1731 **Q. How did Peoples Gas explain the rate base addition of the facility?**

1732 A. When asked to explain “whether these costs were included in rate base by  
1733 Peoples Gas,” Peoples Gas responded that this “[d]etail is not available.”  
1734 (Peoples Gas’ response to DR Docket No. 12-0299 DAS 10.02(c).) Peoples  
1735 Gas also could not address whether it was added to rate base in Docket No.  
1736 95-0032, which had a future test year of beginning October 1, 1995. (Order,  
1737 Docket No. 95-0032, November 8, 1995.) The station appears to have been  
1738 constructed from December 1995 to June 1996. (Attach. AH, Attachment to  
1739 the Companies Response to Staff DR DAS-16.01) Thus, the station was  
1740 completed and in service prior to that test year being finished. (Attach. AI,  
1741 Companies Response to Staff DR Docket No. 12-0299 DAS-7.01(c).)  
1742 Furthermore, revenues from PNGV Corp. did not begin until October, 1996,  
1743 which was after the test year ended. (Attach. AI, Attachment to the  
1744 Companies Supplemental Response to Staff DR Docket No. 12-0299 DAS-  
1745 7.01(h).) Thus, it is quite possible that ratepayers paid for the station  
1746 construction for the better part of 12 years but did not receive any benefit  
1747 from the revenues paid by PNGV Corp. However, even if Peoples Gas

1748 ratepayers never paid for this station construction, it is not in the public  
1749 interest for Peoples Gas to subsidize its affiliates.

1750

1751 **Q. Please summarize your conclusions regarding the evidence about the**  
1752 **PNGV Corp. CNG station.**

1753 A. Peoples Gas provided services for which it did not receive full, reasonable  
1754 cost compensation. The interactions described above between Peoples  
1755 Gas and PNGV support my conclusion that Peoples Gas acted contrary to  
1756 the public interest.

1757

1758 **VI. Conclusion**

1759 **Q. What do you conclude about the Companies interactions with their**  
1760 **affiliates?**

1761 A. The Companies have a history of abuses of the public interest that require  
1762 the Commission to act to protect the public interest going forward. In  
1763 particular, Peoples Gas has acted against the public interest as follows:

- 1764 1. Peoples Gas provided services for PNGV Corp. under the  
1765 Intercompany Service Agreement ("ISA") that was not provided at  
1766 cost as required.  
1767 2. Peoples Gas interacted with Pinnacle preferentially before it  
1768 became an affiliate.  
1769 3. Peoples Gas interacted with Pinnacle after it became an  
1770 affiliate under an agreement that had not been approved by the  
1771 Commission.  
1772 4. Peoples Gas interacted with Pinnacle under the STA after it  
1773 became an affiliate but before it was properly added to the STA.



5. Peoples Gas interacted with Integrys Transportation Fuels after it became an affiliate but before it was properly added to the STA.

6. Peoples Gas attempted to include in its rates costs for PPP solicitation services provided by IBS at no charge to PEHS.

7. Peoples Gas charged PEHS PPP billing charges below cost by not increasing those charges when postage rates increased.

8. Peoples Gas increased charges for repairs to customer-owned piping to ratepayers more than double its costs and charged PEHS PPP repairs charges at cost. This provided PEHS with a competitive advantage by disadvantaging ratepayers.

9. Peoples Gas discriminated against ratepayers who did not purchase PPP in the provision of repairs to customer-owned piping by providing firm repairs services to PEHS but not ratepayers without PPP.

Similarly, North Shore has acted against the public interest as follows:

1. North Shore attempted to include in its rates costs for PPP solicitation services provided by IBS at no charge to PEHS.

2. North Shore charged PEHS PPP billing charges below cost by not increasing those charges when postage rates increased.

3. North Shore increased charges for repairs to customer-owned piping to ratepayers more than double its costs and charged PEHS PPP repairs charges at cost. This provided PEHS with a competitive advantage by disadvantaging ratepayers.

4. North Shore discriminated against ratepayers who did not purchase PPP in the provision of repairs to customer-owned piping by providing firm repairs services to PEHS but not ratepayers without PPP.

**Q. What do you recommend regarding the Master AIA?**

A. I strongly believe that the current set of AIAs does not adequately protect the public interest and that modifications are necessary to prevent further abuse. I recommend that the Commission increase its oversight of these

1808 transactions going forward. Therefore I have the following  
1809 recommendations for the Commission:

1810 Rec. 1. Require that the Master Affiliated Interest Agreement ("Master  
1811 AIA"), that was approved in Docket No. 10-0408 be modified by adding a  
1812 Rider applicable to all Integrys Utilities in Illinois which stipulates that the  
1813 Companies will only provide services to and receive services under the  
1814 Master AIA from regulated affiliates (as outlined in Section C.I) and the  
1815 Companies will not provide services to nor receive services from  
1816 unregulated affiliates (as outlined in Section C.II). Thus, any interactions  
1817 with any unregulated affiliates, apart from the IBS Regulated AIA, would  
1818 require direct Commission approval.

1819 Rec. 2. Prohibit any affiliate or its agent from using information,  
1820 including but not limited to ratepayer lists, received or developed pursuant to  
1821 the provision of services to the Companies from soliciting, marketing or  
1822 otherwise attempting to provide any product or service directly or indirectly to  
1823 the Companies' ratepayers or providing such information to any third party  
1824 whether affiliated with the Companies or not.

1825 Rec. 3. Consider whether fines should be imposed upon the  
1826 Companies for specific Company actions set forth below which violated the  
1827 Act to discourage future improprieties by the Companies and/or other  
1828 utilities.

1829

1830 **Q. Will your first recommendation significantly affect the Companies**  
1831 **operations?**

1832 A. No. The Companies have indicated that this change to the Master AIA  
1833 would not have a substantial impact on their operations because the  
1834 Companies receive most of their services from IBS under the IBS Reg  
1835 AIA. (Attach AM, Companies Response to Staff DR DAS-15.11(a), (b).)  
1836 The only services that they currently receive under the Master AIA are the

1837 maintenance service that ITF performs on the Division Street CNG  
1838 Station. (Attach AM, Companies Response to Staff DR DAS-15.11(d).)

1839

1840 **Q. Does this conclude your prepared direct testimony?**

1841 A. Yes.